Director Liability In Insolvent Companies

An analysis of the effectiveness of private and public enforcement mechanisms with special reference to improper trading liability and disqualification.

Lancaster University
Law School

BENJAMIN ARCHER, LL.B (Hons)
Barrister, of Lincoln's Inn

This thesis is submitted in partial satisfaction of the requirements for the degree of Doctor of Philosophy.

December 2017

For mum and dad, with all my love.

DECLARATION

This thesis, either in whole or in part, has not been submitted in support of an application for another degree at this or any other university.

The substantive arguments and a portion of the text presented in Chapters 2 and 3 of this thesis – pertaining to compensation orders and undertakings, following the introduction of the Small Business, Enterprise and Employment Act 2015 – were delivered to an audience at the Society of Legal Scholars Annual Conference (September 2015, York).

Data was gathered and analysis conducted up until 1 August 2017.

Benjamin Archer

ABSTRACT

Director Liability In Insolvent Companies

An analysis of the effectiveness of private and public enforcement mechanisms with special reference to improper trading liability and disqualification.

BENJAMIN ARCHER, LL.B (Hons)
Barrister, of Lincoln's Inn

December 2017

Encouraging entrepreneurship and trade by permitting free access to limited liability is a cornerstone emblem of UK enterprise policy. However, it comes at a price. The abuse of limited liability by dishonest, unscrupulous, incompetent, negligent, and occasionally deranged directors, who drive a company into insolvency – and the potential that it has to wreak financial havoc upon unsuspecting creditors – is all too well known. Yet, the state's response to this abuse is not to limit access to limited liability. Instead, it has been, over a number of years, to create a wide-ranging regulatory regime in an effort to crack down on directorial misconduct.

The mechanisms employed by the state for this purpose can crudely be split into two camps: 'private' and 'public' enforcement mechanisms. Those in the former category are powers of an insolvency officeholder under the Insolvency Act 1986, and have the primary effect of compensating creditors for misconduct that they have suffered at the hands of delinquent directors. This thesis turns its focus on wrongful and fraudulent trading. Public enforcement in this context means directors' disqualification, pursuant to the Company Directors Disqualification Act 1986.

The need for regulation, whether public and private, is shown to arise as a result of moral hazards created by this laissez-faire approach to accessing limited liability. The regulatory regime and limited liability are therefore inextricably linked. With that in mind, the thesis explores how effective these mechanisms are in preventing abuse. Effectiveness here is determined with reference to the original rationale and underpinning objectives of each respective mechanism. The thesis will however not confine itself to a doctrinal analysis of the mechanisms in pursuit of that aim. It will go further and introduce substantial empirical data, so as to understand their operation 'on the ground' insofar as is possible. It will be shown that each mechanism suffers its own significant difficulties which are inhibitive of their overall effectiveness. Ultimately the author will express the view that none of the mechanisms discussed appear to be working as intended. The thesis examines the recent reforms to this area following the Small Business, Enterprise and Employment Act 2015, but asserts that in reality they are likely to be of minimal significance.

The final part of the thesis criticises the approach of the state in adopting an *ex post facto* system of regulation in the first place. It argues it to be misguided and inevitably resigned to at least partial failure because it does not deal with the underlying problem. The thesis therefore comes full circle in its conclusions by proposing for consideration a new, *ex ante*, alternative that deals with the issues at source: *the curtailment of access to limited liability*.

ACKNOWLEDGEMENTS

Professor David Milman
Mrs Loretta J Archer
Mr George W Archer
Miss Aimée L Brown
Dr John Tribe
My friends and colleagues at Lancaster University Law School
Lonsdale College, Lancaster University
The Dowager Countess Eleanor Peel Trust

You have my eternal gratitude

CONTENTS

LIST OF ABBREVIATIONS

IS	Insolvency Service
CH	Companies House
SS	Secretary of State
DBIS	Department for Business, Innovation and Skills
DTI	Department for Trade and Industry
DBEIS	Department for Business, Energy and Industrial Strategy
PAC	Public Accounts Committee
NAO	National Audit Office
HMRC	Her Majesty’s Revenue and Customs
IP	Insolvency Practitioner

TABLES AND FIGURES

Tables

Figures

TABLE OF CASES

Amgbah v Law Society [2010] EWHC 2183

Atlantic Computers Plc, Re (Ch D, 15 June 1998)

Attorney General of Zambia v Meer Care & Desai (A Firm) [2007] EWHC 952 (Ch)

Austinsuite Furniture Ltd, Re [1992] BCLC 1047

Aviva Insurance Ltd v Brown [2011] EWHC 362

Barings Plc, Re [1998] Ch 356

Barings Plc (No 5), Re [1999] 1 BCLC 433

Blackspur Group Plc (No. 2), Re [1998] BCC 11 (CA)

Brooks v Armstrong [2015] BCC 561; [2016] EWHC 2893 (Ch)

C U Fittings Ltd, Re (1989) 5 BCC 210

Carecraft Construction Co Ltd, Re [1994] 1 WLR 172

Cedarwood Productions Ltd, Re [2004] BCC 65 (CA)

Centros Ltd v Erhvervs-og Selskabsstyrelsen (ECJ Case 212/97) [1999] 2 CMLR 551

Chartmore Ltd, Re [1990] BCLC 673

Cladrose Ltd, Re [1990] BCC 11

Continental Assurance, [2001] BPIR 733

Coventry v Lawrence [2015] UKSC 50

Crestjoy Products Ltd, Re [1990] BCC 23

Cubelock Ltd, Re [2001] BCC 523

Dawes and Henderson (Agencies) Ltd, Re [2000] BCC 204

Dominion International Group Plc, Re [1995] 1 WLR 649

Douglas Construction Services Ltd, Re (1988) 4 BCC 553

El Ajou v Dollar Land Holdings plc [1994] BCC 143

Grayan Building Services Ltd, Re [1995] Ch 241 (CA)

Ipcon Fashions Ltd, Re (1989) 5 BCC 773

Komerçni Banka AS v Stone & Rolls Ltd [2003] 1 Lloyd's Rep 383

Lo-Line Electric Motors Ltd, Re (1988) 4 BCC 415

Melcast (Wolverhampton) Ltd, Re [1991] BCLC 288

Mond v Hyde [1999] QB 1097

Moorgate Metals Ltd, Re [1995] 1 BCLC 503
Morris v Bank of India [2005] EWCA Civ 693
NCG Trading Ltd, Re [2004] EWHC 3203
Oasis Merchandising Services Ltd, Re [1995] BCC 911; [1995] 2 BCLC 493
Official Receiver v Stern [2000] WLR 2230 (CA)
Pamstock Ltd, Re [1994] BCC 264
Pantmaenog Timber Co Ltd, Re [2004] 1 AC 158
Paton v Martin [2016] SC AIR 57
Patrick and Lyon Ltd, Re [1933] Ch 786
Polly Peck International (No 2), Re [1993] BCC 890
Premiermotor Auctions Limited v PWC LLP and Lloyds Bank plc [2016] EWHC 2610 (Ch)
Produce Marketing Consortium Ltd, Re (1989) 5 BCC 569
Purpoint Ltd, Re [1991] BCLC 491
R v Cobbey (1992) 14 Cr App Rep S 82
R v Edwards [1998] 2 Cr App R S 213
R v Evans [2000] BCC 901 (CA)
R v Ghosh [1982] QB 1053
R v Lockwood [1986] 2 BCC 99333
R v Paul Ward [2005] EWCA Crim 1926
Ralls Builders Limited (No. 2), Re [2016] EWHC 1812 (Ch)
Ralls Builders Limited, Re [2016] EWHC 243 (Ch)
Royal Brunei Airlines Sdn Bhd v Tan [1995] 2 AC 378
Ruttle Plant Hire Ltd v SSEFRA (No. 3) [2008] EWHC 730 (TCC)
Salomon v A Salomon & Co Ltd [1896] UKHL 1
Scott v Commissioner of Police of the Metropolis [1974] 3 WLR 741, 819
Sevenoaks Stationers (Retailer) Ltd, Re [1991] Ch 164 (CA); [1990] BCC 765
Smith v UIC Insurance Co Ltd [2001] BCC 11
Southbourne Sheet Metal Co Ltd, Re [1993] WLR 244 (CA)
SSBIS v Brandon Weston, Christopher David Williams [2014] EWHC 2933 (Ch)
SSTI v Bannister [1995] BCC 1027
SSTI v Creegan [2002] 1 BCLC 99
SSTI v Hickling [1996] BCC 678

SSTI v Jeffrey Albert Vane (Ch D, 30 June 1997); [1997] WL 1104724

SSTI v Tjolle [1998] BCC 282

Stanford Services Ltd, Re (1987) 3 BCC 326

Swift 736 Ltd, Re [1992] BCC 93; [1993] BCC 312

Twinsectra Ltd v Yardley [2002] UKHL 12

Ultraframe (UK) Ltd v Fielding [2005] EWHC 1638 (Ch)

Verby Print for Advertising Ltd, Re [1998] BCC 652, 665.

Wedgecraft Ltd, Re (unreported) 7 March 1986

Westmid Packing Services Ltd, Re [1998] 2 All ER 124; [1998] BCC 836

William C Leitch Brothers Ltd, Re [1932] 2 Ch 71

TABLE OF LEGISLATION

United Kingdom

Primary Legislation

Access to Justice Act 1999

Companies Act 1929

Companies Act 1947

Companies Act 1976

Companies Act 1985

Companies Act 2006

Company Directors Disqualification Act 1986

Court and Legal Services Act 1990

Insolvency Act 1985

Insolvency Act 1986

Insolvency Act 2000

Legal Aid, Sentencing and Punishment of Offenders Act 2012

Powers of Criminal Courts (Sentencing) Act 2000

Small Business, Enterprise and Employment Act 2015

Statutory Instruments

The Companies (Disqualification Orders) Regulations 2009, SI 2009/2471

The Conditional Fee Agreements Order 1995, SI 1995/1674

The Insolvent Companies (Report on Conduct of Directors) Rules 1996, SI 1996/1909

The Insolvent Companies (Reports on Conduct of Directors) (Amendment) Rules 2001, SI 2001/764

The Insolvent Companies (Reports on Conduct of Directors) (England and Wales) Rules 2016, SI 2016/180

The Legal Aid, Sentencing and Punishment of Offenders Act 2012 (Commencement No. 5 and Saving Provision) Order 2013, SI 2013/77

The Legal Aid, Sentencing and Punishment of Offenders Act 2012 (Commencement No. 12) Order 2016, SI 2016/345

The Small Business, Enterprise and Employment Act 2015 (Commencement No. 2 and Transitional Provisions) Regulations 2015, SI 2015/1689

Australia

Primary Legislation

Corporations Act 2001

Part I

INTRODUCTION

1

INTRODUCTION

1.1 The limited liability company has been deified by some commentators as a 'miracle'[1] and 'one of the most ingenious concepts ever devised'.[2] Yet, at the other end of the spectrum of opinion, it has been described as a creation akin to Frankenstein's monster,[3] or the product of 'one of Alice's more extreme adventures on her sojourn in Wonderland'.[4] There is little doubt, however, that in modern enterprise culture the limited company is of crucial importance in facilitating and encouraging entrepreneurship.[5] The idea that even a 'one-man' concern is able to incorporate at minimal cost, and with few requirements,[6] is seen as pivotal.[7] Moreover, it is the enterprise policy of the UK that business failure is to be expected and entrepreneurs should not be condemned, or face stigmatisation, for this fact alone. Instead, a culture of business rescue and recovery continues to be exalted.[8] It has always been the case,

[1] Colin Meyer, *Firm Commitment: Why the corporation is failing us and how to restore trust in it* (Oxford University Press 2013) 21.
[2] ibid.
[3] Maurice Wormser, *Frankenstein, Incorporated* (McGraw-Hill Book Company 1931) 85.
[4] ibid 93.
[5] For the financial year 2016-17 there were 605,951 private companies incorporated in England and Wales (and 408,563 dissolutions). See Companies House, 'Companies Register Activity in the United Kingdom 2016-2017' (2017) <http://bit.ly/2vbSQg2> accessed 1 August 2017, Table A2.
[6] See ch 6.
[7] DTI, *Modernising Company Law* (White Paper, Cm 5553, 2002). In particular note Part II, 'The Right Approach to Small Companies'.
[8] See generally Gerard McCormack, *Corporate Rescue Law – an Anglo-American Perspective* (Edward Elgar 2008), ch 2.

however, that with the economic advantages that limited liability brings, both to the entrepreneur and to wider society, there are commensurate disadvantages that arise as a result of the way in which it can be abused. This is because limited liability permits, in effect, the risk of trading to be passed on to creditors of the company.[9] It therefore brings about an opportunity for unscrupulous individuals to exploit the corporate structure by running up large debts that are unable (if they were ever intended) to be paid, at 'limited' risk to their personal assets. This opportunity can prove to be a temptation too great for the fraudster to resist. Similarly, even for the delinquent or the sheer incompetent entrepreneur, it is a structure easily capable of negligent or ignorant abuse. And, as history has shown, those who control companies in such a manner can often escape liability, by hiding behind the corporate veil, simply to repeat the process *ad infinitum*.[10] During periods of boom, directors will therefore carry on the business to derive potentially unlimited profits for shareholders. However, when in more choppy waters, by the time any of this misconduct or impropriety is discovered it is often too late: the company is already well into the 'twilight zone'[11] or insolvent, and unsecured creditors will invariably see little, if any, return.

1.2 Yet, successive governments have been especially wary of inhibiting access to limited liability in any shape or form, largely because of the strongly held perception that it stimulates economic growth and encourages entrepreneurship.[12] In more recent

[9] This concept will be dealt with in more depth below: 1.6.
[10] A process known in the insolvency community as 'phoenixism': David Milman, *Governance of Distressed Firms* (Edward Elgar 2013) 58-59.
[11] This term is widely utilised in the insolvency literature to refer to companies that are insolvent, or of doubtful solvency, even though they are not in a formal insolvency regime. See generally Milman, (ibid) ch 3.
[12] See for instance Aubrey L Diamond, 'Corporate Personality and Limited Liability' in Tony Orhnial (ed), *Limited Liability and the Corporation* (Croom Helm 1982).

times, however, in part due to moral outrage, the abuse of limited liability has been subject to increased scrutiny. The state has began to engage in an exercise of weighing the benefits of wealth creation against the cost of failed enterprise. Thus, a regulatory regime, aimed at 'cracking down'[13] on delinquent managers, was born to ensure that the market, and the public at large, are protected from those who choose to abuse the privilege of limited liability. Doing so – and doing so successfully – is seen as a key measure of public trust and confidence in the insolvency regime.[14] Directors have executive authority over, and responsibility for, the day-to-day activities of a corporation. It is therefore unsurprising that they are a prime target for regulation aimed at tackling improper conduct. What results is a somewhat fragile balance that has to be retained between the state wishing to encourage trade and enterprise on the one hand, but on the other ensuring that legal regulatory mechanisms are satisfactory so as to prevent the abuse of limited liability. This is to protect stakeholders, including creditors, and ultimately to ensure public confidence is maintained in the corporate form.[15]

1.3 The state's answer to preserving this balance exists in a series of *ex post facto* regulatory mechanisms. For convenience, these may be roughly divided into two streams of enforcement: 'private' and 'public'. The operation of private mechanisms

---

[13] The terminology used by Sir Vince Cable during his time as Business Secretary. There has indeed been a great deal of political rhetoric on the issue over the years. See for example Rowena Mason, 'Vince Cable to bring in tougher penalties for dodgy directors' *The Guardian* (19 April 2014) <http://bit.ly/2q6crfL> accessed 17 May 2016; BBC News, 'Vince Cable proposes tougher rules for directors' *BBC Online* (15 July 2013) <http://bbc.in/2rGgX51> accessed 17 May 2016; David Oakley and Helen Warrell, 'UK to crack down on negligent directors' *Financial Times* (14 July 2013) <http://on.ft.com/2vtPmGY> accessed 17 May 2016.

[14] DBIS, 'Transparency and Trust: Enhancing the Transparency of UK Company Ownership and Increasing Trust in UK Business – Discussion Paper' (July 2013) <http://bit.ly/1F8U9Ks> accessed 18 October 2015, Executive Summary (T&T Discussion Paper).

[15] See, for example, NAO, *Report by the Comptroller and Auditor General: Insolvency Service Executive Agency, Company Director Disqualification – A Follow Up Report* (HC 1998-1999, 424) Executive Summary (NAO Follow-Up Report).

generally takes the form of rendering the delinquent manager (or other person as the case may be) personally liable for the debts of the company so caused by her misconduct. They are proceedings invariably commenced by a liquidator or administrator of the insolvent company, utilised as a means of swelling the pool of assets available for creditors.[16] The private mechanisms discussed in this thesis are wrongful trading and fraudulent trading (collectively 'improper trading'), pursuant to sections 213 and 214 of the Insolvency Act 1986 ('IA 1986') respectively. The essence of public regulation in this sphere, however, is 'disqualifying' the person in question from being involved in the management of companies, for a fixed period of time, pursuant to the Company Directors Disqualification Act 1986 ('CDDA 1986').[17] Public enforcement proceedings are of course taken by the state itself, either by pursuing a court order, or seeking an undertaking from the individual that she will not act in a proscribed manner for the period of disqualification. As will be demonstrated throughout the course of this thesis, all of these mechanisms have seen significant, recent, reform as a result of the Small Business, Enterprise and Employment Act 2015 ('SBEEA 2015').

QUESTIONS FOR RESEARCH

1.4 With the scene set, the focus will turn to the purpose of this thesis. In essence, it sets out to explore the following research questions:

> (a) with a special focus on improper trading and disqualification in English law, how effective is the current civil regulatory regime in dealing with rogue directors of insolvent companies?

[16] See chs 4-5.
[17] See chs 2-3.

(b) in so far as is possible to determine, what impact might the new measures introduced by the Small Business, Enterprise and Employment Act 2015 ('SBEEA 2015') have upon the effectiveness of the mechanisms subject to discussion?

(c) what further measures might be taken, or reforms implemented, in order to improve the effectiveness of individual mechanisms and the regime overall?

(d) given that the abuse of limited liability creates the need for regulation, what measures might be taken, or reforms implemented, to reduce abuse, thereby tackling the problem at source and minimising the need for reliance on enforcement mechanisms?

In order to lay the groundwork for doing so, this chapter will now turn to deal with some preliminary matters: to explain some core concepts and ideas in more detail; to set out the justification for the inquiry to be conducted; and to explore the way in which the author will do so, and the methodology adopted.

Defining and Questioning 'Effectiveness'

1.5 Given the questions just posed, it is of course central to the forthcoming analysis that the reader has an appreciation for how 'effectiveness' or 'success' are to be determined in this context. The author has chosen to define effectiveness, as have other commentators in this area[18] – either explicitly or implicitly – in the following terms. An *effective* mechanism is one which accords, both in theory and in practice, with its original mandate and objectives. A mechanism that adheres to its underlying objectives is one which, it will be argued, ought to be considered a *success*. Conversely, where it is identified that these aims do not mirror implementation, it will be argued that this is evidence of (at least partial) failure or ineffectiveness. Given the statutory footing of the enforcement mechanisms discussed, the objectives are those as elicited by Parliament, the Government in consultation, or, where relevant, as developed by the courts. More

[18] For instance, Andrew Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (ACCA Research Report 59, 1998); Richard Williams, *Disqualification Undertakings: Law, Policy and Practice* (Jordans Publishing Limited 2011); T&T Discussion Paper (n 14).

broadly, and quite separately, it is argued here that any evidence revealing a lack of stakeholder trust and confidence – either in the regime generally or in relation to individual mechanisms – must also impinge upon success. Thus, even in the hypothetical situation where a mechanism is operating entirely in accordance with its objectives, should public trust and confidence in it be low, then, put simply, it cannot be said to be successful. This approach is taken for two reasons. First, 'public trust and confidence' is a metric routinely used by the state itself in order to assess effectiveness of the enforcement regime. Second, low confidence in a mechanism may arise if it is not operating effectively. However, it may also arise where there are wider concerns within the enforcement regime itself – beyond the simple objectives themselves – deserving of examination.

THE NEED FOR REGULATION

The Problem Is Limited Liability

1.6 More ought to be said as to why regulation, whether private or public, is seen as necessary or even desirable in the first place. It has already been stated that, at the most basic level, its function is to curtail the effects of the abuse of limited liability. This warrants further explanation at this juncture. In order to do so, some of the fundamentals, both legal and economical, must be set out to properly frame the arguments that follow. It is trite that limited liability forgoes shareholders from having to imperil their own personal assets, save for the paid-up value of their shares. In other words, shareholders can cap their liability to a known and fixed amount in advance, unilaterally, as they see fit. Because of this a moral hazard[19] problem arises.

[19] This is an economics term, defined by the Oxford English Dictionary as the 'lack of incentive to guard against risk where one is protected from its consequences'.

Shareholders are incentivised to cause the company to engage in more risky trading activities, in the hope of greater returns. The state's position is that it is the participation in this risk that encourages economic growth.[20] If the business were to become insolvent, and ultimately fail, the shareholder has lost her investment; but no more and no less. It therefore follows that, in insolvency, a shareholder who injects more capital suffers greater losses. In turn, this ought to reduce any moral hazard, as more is a stake. Yet, in relation to private companies, there are no minimum capital requirements under English law.[21] As such, it will come of little surprise to the reader that the vast majority of companies choose to incorporate with a share capital of less than £100; many with a single pound. On that basis, a moral hazard will usually arise from the very moment of the company's inception, becoming intensified where the company enters the twilight zone or is insolvent. By way of contrast, in a system of unlimited liability moral hazards are less pronounced. Entrepreneurs are more likely to be risk averse and prudent in their commercial activities as, in the event of failure, their own personal assets are in jeopardy and bankruptcy may ultimately follow.[22] In either case, however, the risk is not eliminated, as Bainbridge and Henderson note.[23] The difference is that where an entrepreneur is subject to a regime of unlimited liability the loss remains fixed with her, save in cases where the parties decide to contract *in* to limited liability on a per-transaction basis. She can be pursued by creditors, who may routinely seek recovery

[20] Stephen M Bainbridge and Todd Henderson, *Limited Liability: A Legal and Economic Analysis* (Edward Elgar 2016) 47.

[21] Banks are a known exception to this general rule. For detail see: Sarah Garvey and others, *Encyclopedia of Banking Law* (LexisNexis UK 1996) div A, ch 5. Public companies of course must have a minimum capital of £50,000 by virtue of Companies Act 2006 (CA 2006), s 763.

[22] See Paul Halpern, Michael Trebilcock and Stuart Turnbull, 'An Economic Analysis of Limited Liability in Corporation Law' (1980) UTLJ 30 117, 127 who, rather interestingly, notes that ultimately of course an individual always has *de facto* personal limited liability in view of the very fact that one can declare oneself a bankrupt.

[23] Bainbridge and Henderson (n 20) 47-48.

against personal assets. In a system of limited liability, however, risk is *shifted* on an uncompensated basis. In short, the loss falls to the feet of the company's creditors and, unless security has been obtained, there the loss will invariably remain. In the language of economics, limited liability therefore creates negative externalities, with the incumbent risk of trading (at least in part) being shifted to creditors of the company.[24] However, contrary to what has just been said, Posner has argued that limited liability in fact does not cause an uncompensated transfer of risk.[25] The substance of that argument is as follows. Because limited liability exists as a default rule, all those who transact with the company can be presumed to know the inherent risks of doing so. Creditors will therefore compensate for that risk of default either by requiring the contracting-out of limited liability, or by increasing rates of interest. This forces the risk of default to be internalised by shareholders. However, as Prentice argues, this clearly has no application to involuntary creditors who, by definition, cannot choose to whom they extend credit, nor its precise terms.[26] Moreover, Prentice suggests that even voluntary creditors may be subject to the uncompensated transfer of risk in insolvency situations, as shareholders 'cease to have any material interest in the assets of the company',[27] incentivising further risk taking. He puts it in the following way:

> In a situation of insolvency, the shareholders have a perverse incentive to continue the company in business since they have everything to gain and nothing to lose. Any additional loss will be at the expense of the creditors, and should the company trade back into solvency the gains will be appropriated by the shareholders. In other words, there is no downside risk but only upside advantage.[28]

[24] ibid 49.
[25] Richard Posner, 'The Rights of Creditors of Affiliated Corporations' (1967) 43 U Chi L Rev 499.
[26] Dan D Prentice, 'Corporate Personality, Limited Liability and the Protection of Creditors' in Ross Grantham and Charles Rickett (eds), *Corporate Personality in the Twentieth Century* (Hart Publishing 1998) 104.
[27] ibid 105.
[28] ibid.

The role of regulation is therefore clear. It seeks to control the most egregious exercises of this risk transfer process, which results from dishonest, negligent, incompetent or ignorant behaviour. Private regulation aims to give confidence to the market that those who behave irresponsibly are not beyond reproach, and can be dealt with accordingly. Public regulation goes further, recognising that in some instances the privilege of limited liability ought to be withdrawn entirely in order to protect the market, and the wider public, on economic grounds. In either case, the response of the state to abuse is not to compromise its position that limited liability must be as freely available as possible.[29] Instead, it simply tightens its regulatory grip.

Who Should Be Regulated?

1.7 If this potential for abuse is accepted as the reason for regulation, a separate but interrelated question arises as to precisely which actors can be said to be responsible for the abuse, and therefore *who* ought to be regulated. Prentice identifies three 'constituencies' from whom recovery could be sought in most cases: creditors, shareholders and directors.[30] The discussion in this thesis deals with only one of these; namely directors. However, it should be recognised that a number of avoidance mechanisms exist that permit an insolvency officeholder to pursue *creditors* for contributions to the insolvent company's assets in given circumstances.[31] On the other hand, there is comparably little appetite for the view that shareholders ought be pursued

---

[29] For instance, by imposing minimum share capital rules or other 'entry requirements'; the merits of which are discussed in the penultimate chapter. The state's position must be that this is preferable economically, in spite of the potential for abuse, to the reverse position; i.e. where limited liability must be contracted *in to* on a per transaction basis. Presumably, due to the existence of transaction costs.

[30] The phrase used by Prentice (n 26) 99.

[31] For instance, where there have been transactions at an undervalue: Insolvency Act 1986, s 238 (IA 1986) or preferences: IA 1986, s 239.

to contribute any more than the value of their unpaid shareholdings. The simple reason for that, following on from the previous discussion, is that to do so would be to subvert limited liability. Kempin has argued, more fundamentally, that to impose additional liabilities on shareholders would be 'unfair'[32] as it would make:

> …the shareholders liable for what they cannot directly control. The only control shareholders can have over the acts of the directors is after the fact – that is, they can refuse to re-elect them if they determine that there has been mismanagement…In addition, the shareholders are harmed by the mismanagement of the directors and officers at least as much as are the creditors. They may even be injured more than the creditors are injured, for they do not, almost by definition, receive the return of any of their invested capital until the outside creditors have been satisfied.[33]

1.8 *Why do directors act improperly?* The prevailing theory is that in a system of corporate governance that splits management and ownership, directors may tend towards negligent or self-serving behaviour by virtue of their agency. Jensen and Meckling, in their seminal work on the theory of the firm, describe directors and shareholders as being in 'pure agency relationship'[34], which they argue can lead to agency problems:

> If both parties to the relationship are utility maximizers there is good reason to believe that the agent will not always act in the best interests of the principal. The *principal* can limit divergences from his interest by establishing appropriate incentives for the agent and by incurring monitoring costs designed to limited the aberrant activities of the agent…In most agency relationships…there will be some divergence between the agent's decisions and those decisions which would maximize the welfare of the principal.[35]

It is recognised in corporate governance literature that an underlying purpose of the corporation, and therefore one of the primary obligations of directors, is to increase

[32] Frederick G Kempin, 'Limited Liability in Historical Perspective' (1960) 4(1) ABLA Bulletin 32.
[33] ibid. However, clearly, this has little application in the case of the owner-managed firm.
[34] Defined as 'a contract under which one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent': Michael C Jensen and William H Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3 JFE 305, 308.
[35] ibid.

shareholder value.[36] However, being utility maximisers and the managers of other peoples' money,[37] directors are incentivised to engage in risky trading behaviours or self-dealing for their own benefit. They do so in the knowledge that, should the venture fail, there is minimal risk to themselves and to shareholders, due to the principles of separate legal personality and limited liability. In an effort to curtail managerial 'negligence and profusion'[38] directors are subjected to a multitude of statutory duties.[39] At their roots, the mechanisms explored in this thesis (and more broadly) are designed to complement those duties, by creating enforcement powers, should a director fail to adhere to them. Moreover, it is generally recognised that shareholders will engage in the monitoring of directors.[40] Whilst this has an intrinsic cost it may benefit the shareholder in the longer term by reducing the scope for abuse that may ultimately cause insolvency, and a total loss of the investment.[41] External monitoring mechanisms, for instance statutory auditing, also have a role to play.[42] However, the very existence of regulation, it is argued, suggests that monitoring is incomplete as a solution. For instance, in the case of the owner-managed corporation, it is suggested that the above analysis is of limited application. Owner-managers are especially important in the context of this thesis as the lion's share of enforcement action is, in fact, taken against

---

[36] Meyer (n 1) 67. To fail to do so may be a breach of duty to promote the success of the company, pursuant to s 172 CA 2006. However, attitudes have shifted towards other pressing concerns such as environmental sustainability. See generally, Benjamin J Richardson and Beate Sjåfjell (eds), *Company Law and Sustainability: Legal Barriers and Opportunities* (CUP 2015).
[37] Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (MetaLibri Digital Edition 2007), 574.
[38] This was considered by Smith, ibid 574, to be almost an inevitability, given that directors are 'the managers rather of other people's money than of their own'.
[39] Namely those set out in the CA 2006, ss 171-177.
[40] Jensen and Meckling (n 34) 305.
[41] ibid 308-310.
[42] Pursuant to CA 2006, pt 16. However, CA 2006, s 477 provides that 'small' private companies, as defined by CA 2006, s 382, are exempted from audit requirements. As such, for the vast majority of corporations, this type of statutory monitoring has no application.

that demographic.[43] For reasons about to be stated, this is entirely unsurprising. In an owner-managed company, the directors and shareholders are materially the same person(s), and thus the economic (though not the legal) reality is the entrepreneur is managing her own money. In line with the words of Jensen and Meckling above,[44] therefore, the owner-manager will take decisions solely to maximise *her own* utility. But, she does so in circumstances where there is a total absence of monitoring. The owner-manager is accountable only to herself, and therefore misconduct as against creditors or general delinquency in the conduct of her office is likely to go unchecked. She therefore faces little scrutiny but, due to the moral hazard created by limited liability, is incentivised to carry on trading in a potentially imprudent manner.[45] In other cases, even where ownership and management are truly separated, monitoring may similarly be absent; inadequate; or directors may simply find that they are insufficiently incentivised to stay on the straight and narrow. In any of these instances, the original problem is returned to. And therein lies the justification for regulation: in the words of Mayer 'neither incentives nor reputations can be relied on to align the interests of companies with those of society more generally…[therefore] we turn to third parties, namely governments and regulators to do this for us'.[46]

Private or Public Regulation?

1.9 Given this thesis' compartmentalisation, into 'private' and 'public', of the enforcement mechanisms to be considered, some words ought to be devoted to the

[43] 3.47
[44] Jensen and Meckling (n 34) 312.
[45] This is a criticism of considerable antiquity. See for instance the work of Otto Kahn-Freund, 'Some Reflections on Company Law Reform' (1944) 7 MLR 54, where he was heavily critical of the application of the *Salomon* principle in relation to so-called 'one-man' companies.
[46] Meyer (n 1) 68.

interaction between the two. The very existence of public regulation in UK company law is a curiosity. There has been considerable academic discussion as to the merits or desirability of having a system public regulation whatsoever.[47] It is not the intention of the author to delve into such matters in any great detail. The purpose of this thesis is to consider whether the private and public enforcement mechanisms, as they stand, are effective. It is not, however, to assess the merits of a regulatory system that is private, public, or a combination of the two, in the abstract. Keay, however, has noted that in recent times the state has charted a course which demands that 'there should not be too much regulation and that corporate governance should be seen generally as self-regulatory'.[48] One of the primary anti-public regulation arguments, he suggests, is that as companies are 'effectively private…the law, the enforcement of it and relevant remedies should also be private'.[49] Yet, it is submitted, the position must change where companies become insolvent. It has long been recognised that there is a public interest element to insolvency proceedings. The *fact* that companies fail is not necessarily a public interest matter. However, the reason *why* they fail certainly is. As Walton notes, insolvency litigation is in effect tripartite; it involves the claimant, the defendant, and the wider public at large.[50] But, enforcement proceedings taken by the state require dedicated and specialised officers to carry out investigations and conduct prosecutions.[51] These have a cost to the general taxpayer. Private enforcement is therefore *prima facie*

[47] See generally for example, Andrew Keay, 'The Public Enforcement of Directors' Duties: A Normative Inquiry' (2014) 43 CLWR 89; Robert Baldwin, 'The New Punitive Regulation' (2004) 67 MLR 351; Howell Jackson and Mark Roe, 'Public and Private Enforcement of Securities Laws: Resource-Based Evidence' (2009) 93 JFE 207.
[48] Keay (n 47) 94.
[49] Keay (n 47) 93.
[50] See Peter Walton, 'The Likely Effect of the Jackson Reforms – an Empirical Investigation' (An R3 Report, April 2014) <http://bit.ly/2atR1qh> accessed 1 July 2016, 10.
[51] This function is carried out by the Investigations Unit at the IS.

desirable over public enforcement from the perspective of the state, as it reduces or eliminates this cost to the public at large, thereby ensuring that those who benefit from any regulatory action will pay for it.[52] It follows, on economic grounds, that if private regulation in isolation was effective (or was perceived as being effective) in preventing or combating abuse, then there would be no cause for public regulation. A fundamental issue with private regulation, however, is that those with *locus standi* may not be able to take action, for a variety of reasons to be explored in due course, or may simply choose not to.[53] Thus, it can be stated from the outset that private enforcement must be seen (by the state at least) as only a partial solution to remedying abuses of limited liability. Therein lies the rationale and justification of this thesis in assessing its effectiveness. This 'lacuna'[54] in the private enforcement regime, in theory, is filled by public regulation. But due to its own prioritisation of resources, the state cannot reasonably fund all actions in countering abuse. Thus, the thesis will consider how successfully directors' disqualification as a regulatory tool fills this gap, before going on to deal with private enforcement mechanisms.

1.10 Keay advocates that these two separate streams of enforcement ought to work together in harmony, with the aim of improving the overall effectiveness of the UK corporate governance regime.[55] However, the distinction between 'public' and 'private' has in recent times become rather blurred. Private mechanisms of enforcement have been said to have some public function, in that they may deter others from similar

[52] Keay (n 47) 117.
[53] ch 4.
[54] Keay (n 47) 93.
[55] ibid 119.

misconduct.[56] Moreover, following changes introduced by the SBEEA 2015, which permit a court to order,[57] or the SS to seek an undertaking,[58] that a disqualified director pay compensation to creditors,[59] it might readily be argued that disqualification now embodies a core function of the existing private enforcement mechanisms, through its ability to directly compensate creditors. However, the way in which the mechanisms have been compartmentalised in this thesis is justified on the basis that each still can readily identified as having the primary objective of securing either a private or public remedy, as the case may be. This blurring of the lines will be discussed in more detail in due course and, in fact, will be utilised as a means of returning to the original question; i.e. the effectiveness of the various mechanisms in fulfilling their stated objectives. Particularly when considering the SBEEA 2015, it is argued, the willingness of the state to implement reform itself must be the product of a recognition of failure, at least in part, of the enforcement regime to embody its objectives to date. In line with the author's approach, therefore, this has a direct bearing on effectiveness.

METHODOLOGY

The Approach

1.11 Legal doctrine is by no means a singularly faceted discipline. At the very least, it has been recognised as being in part hermeneutic; part axiomatic; and in other parts historical.[60] According to Van Hoecke 'the core business of legal doctrine is

---

[56] ibid 61 (fraudulent trading) and 109 (wrongful trading).
[57] CDDA 1986, s 15A(1).
[58] CDDA 1986, s 15A(2).
[59] 2.34
[60] Mark Van Hoecke, 'Legal Doctrine: Which Method(s) for What Kind of Discipline?' in Mark Van Hoecke (ed), *Methodologies of Legal Research: Which Kind of Method for What Kind of Discipline?* (Hart Publishing 2011) 6.

interpretation',[61] whilst De Geest has argued that its purpose is to reveal an 'empirical truth';[62] defined as being 'what the judge or legislator really meant'.[63] This last statement encapsulates at least part of what underpins this thesis. Understanding what the legislator 'really meant', in terms of the objectives of and rationale for the private and public enforcement mechanisms available, is central to the discussion. This alone, however, is not sufficient for present purposes. Because, merely understanding Parliament's intentions as to how the enforcement regime ought to operate tells us nothing of how it *actually* operates. It is argued that only through determining how it operates in practice, in so far as is possible, can any meaningful discussion as to its effectiveness take place. Van Hoecke describes this approach, i.e. the one adopted by the author, as 'evaluative' in legal methods terminology.[64] He states it as being the process of 'testing whether rules work in practice, or whether they are in accordance with desirable moral, political, economical aims'.[65] It is of note that the thesis does not set out to criticise what the underlying objectives of the mechanisms *are*, i.e. whether morally, politically, economically, socially, legally, they are the correct ones to be pursuing. Instead, it merely explores the effectiveness of the mechanisms, both public and private, with reference to those objectives *whatever they may be.* Much of the existing literature, most certainly due to the breadth of the issues at play, invariably focuses on one individual mechanism, or is confined to either 'private' or 'public'

---

[61] ibid 3 (emphasis added).
[62] Gerrit De Geest, 'Hoe maken we van de rechtswetenschap een volwaardige wetenschap' (2004) Nederlands Juristenblad 58, 59 as quoted in Van Hoecke (tr) ibid 6.
[63] ibid.
[64] Van Hoecke (n 60) v; AHRQ, 'Mixed Methods: Integrating Quantitative and Qualitative Data Collection and Analysis While Studying Patient-Centered Medical Home Models' (PCMH Series, March 2013) available at <http://bit.ly/2fYMFcY> accessed 1 January 2017.
[65] Van Hoecke ibid v.

enforcement. This thesis takes more of an all-encompassing approach in examining the landscape of director liability, across both public and private enforcement mechanisms. Ultimately, this will permit conclusions to be drawn as to the state of the regime in its totality, in so far as is reasonably possible within the confines of the project.

1.12 In pursuit of this task, then, a broad range of methods of inquiry are required. The traditional method of text analysis in legal scholarship, of course, has a dominant role to play in this thesis. In this context, it will involve an hermeneutic analysis, combined with deductive reasoning (e.g. through the use of syllogistic logic) which in turn permits the author to make findings, and draw conclusions, in the usual way. In doing so, at least some attempt can be made in answering the research questions posited earlier in this chapter. Naturally, this will involve the use of sources including primary and secondary legislation; case law; government policy and consultation documents; existing empirical studies; and scholarly publications including journal articles and monographs. The author partly found fortune in that, in the course of conducting the research for this thesis, the law in this area changed somewhat significantly. The SBEEA 2015 brought about reform in an area that had largely remained untouched for two decades; in some cases, three.[66] The problem that lies therein however is that little is known, at the time of writing, as to how these changes will operate in practice. This has in turn led, in respect of the SBEEA 2015, to a purely interpretative methodology based largely on policy and consultation documents. Therefore, the best the author can reasonably do in this context is assess the *potential* effectiveness of the new reforms, as

[66] The former refers to disqualification, where the last substantive innovation came as part of the Insolvency Act 2000 (IA 2000) which introduced disqualification undertakings. The latter refers to wrongful and fraudulent trading, which have not seen any major changes to their operation since their inception in the IA 1986.

when measured against the known failings or inadequacies of the current system. The reader will recognise that this has obvious limitations, in that the analysis conducted in respect of those reforms may not ultimately be reflective of the reality.

1.13 Taking a qualitative approach, it is submitted, is the optimal means of determining the rationale of each enforcement mechanism, as well as in identifying existing criticisms of their operation. This can be done by way of a review of primary and secondary sources. As previously stated, however, this is insufficient to the task at hand. The overall methodology of this thesis, therefore, might be described as an evaluative 'mixed methods' approach.[67] This is one that integrates both qualitative and quantitative elements. In theory, it enables a more thorough observation of findings, and permits new observations that would simply not be possible with the utilisation of a single method. The thesis will therefore not confine itself to a doctrinal or theoretical analysis of the legal sources, it will also employ quantitative methods in answering the research questions posed. This method of inquiry will largely be utilised in relation to the public enforcement mechanism considered, namely disqualification, simply due to the availability of data in that area. Determining effectiveness, it is submitted, is something best informed by the actual operation of a system 'on the ground'. As such, the existing empirical works in this area will be heavily drawn upon in assessing effectiveness. However, as will be demonstrated in due course, the existing studies are either outdated or are more limited in scope than those set out herein. To assist in the process of determining effectiveness, the author sets out his own up-to-date statistical

[67] For a detailed exposition of the advantages and limitations of this approach see AHRQ (n 64) 2-3.

analyses of disqualification, based on secondary data. The particular research design posited here utilises the quantitative analysis in three ways:

(a) to explore new findings in the vein of the effectiveness of directors' disqualification on the whole; as well as to permit the reiteration and reconfirmation of old ones, albeit with more up-to-date source data.

(b) to validate the qualitative findings as to the effectiveness of disqualification (and vice-versa);

(c) to permit further exploration of the qualitative observations, thereby enabling a better understanding of real-world experiences of the disqualification undertakings regime.

The reader will not, at this stage, be troubled with the methodology of the empirical work conducted. The reason for that is straightforward in that, it is submitted, it is most comprehensible when presented *in situ*. As such, any empirical analysis to be undertaken in this thesis will be prefaced with a comprehensive methodology at the relevant point.

Private Enforcement: Thesis Scope

1.14 It should be noted that there are other private mechanisms of enforcement in English law not discussed in this thesis, with the most noteworthy being the summary remedy available to be taken against directors pursuant to section 212 of the IA 1986; commonly known as misfeasance. There are two primary reasons that the author has chosen to focus this work specifically in the area of improper trading. First, because a full and complete exposition of *all* of the legal mechanisms available to pursue directors would be a task that transcends far beyond the scope of a single thesis. It therefore follows that the author had to be selective to some degree. Secondly, it can be said with some certainty that the mechanisms discussed in this thesis – both public and private – are currently at the forefront of government policy in the context of director liability.

This is evidenced by the fact that they have seen *significant* reforms as recent as 2015, pursuant to the SBEEA 2015. For two primary reasons, they therefore make for interesting critique and analysis. First, at the time of writing, how these reforms will take hold is still an emerging landscape, thus providing an opportunity for informed speculation in that regard. Secondly, as will be argued, a will to implement reform, by definition, suggests weakness (or at least perceived weakness) in the existing system. The reforms of the SBEEA 2015 therefore come at an opportune time in the writing of this thesis to explore those past difficulties, as well as in looking to the future. On the contrary, misfeasance has existed more or less in its current form since the late nineteenth century. It is legislatively stagnant and thus, unlike the mechanisms discussed in this thesis, cannot be said to form part of the *modern* (i.e. post-Cork)[68] policy initiatives in this area.

Ethical Considerations

1.15 As has been stated, this thesis draws rather heavily on empirical analysis conducted by the author. A significant part of this analysis involved the collection of biographical data of disqualified directors. Unlike some of the previous studies in this area, which made use of primary data,[69] the author's study solely utilises secondary data. As will be discussed in considerable depth in Chapter 3, this took the form of data obtained from the *public* registers of disqualified individuals provided by two executive agencies of the DBEIS; namely CH and the IS.[70] The extent of the data is plainly invasive. Indeed, this has been recognised by the state, who have sought to reduce or

[68] DTI, *Insolvency Law and Practice: Report of the Review Committee* (Cmnd 8558, 1982) (Cork Report).
[69] For example Hicks (n 18).
[70] 3.5

redact certain parts of the information presented on the public register so as to minimise the risk of fraudulent impersonations by opportunistic criminals.[71] Potential ethical considerations were therefore at the forefront of the author's mind in collecting and analysing the data, as well as in how to manage it following completion of the study. It was considered that the collection of this data for analysis, without the permission of the subjects involved, did not impinge upon any core principles in the conduct of ethical research. Predominantly, this was because the data is, in effect, Government data provided in the public interest under statutory authority. In short, the information used is a matter of public record. Indeed, the naming and shaming of delinquent directors in a public forum – so that their conduct can be scrutinised – is fundamental to at least one of the objectives of disqualification; namely deterrence.[72] It was therefore considered, given this crucial factor, that the present study should not be inhibited by the usual ethical considerations that apply to surveys of this type, where informed consent must be sought. It is submitted that the survey's findings, and their publication, ought themselves to be matter of public interest. The data was not used for any purpose other than for the analysis set out in this thesis.

1.16 However, although publicly available at the time of collection, upon the lapse of individual disqualifications the information held ceases to appear on the official databases. In terms of the storage and retention of the data, therefore, as best practice, the core data protection principles imposed upon Data Controllers pursuant to the Data

[71] For example, a director's *full* date of birth was obscured from the register following the implementation of the Small Business, Enterprise and Employment Act 2015 (SBEEA 2015), s 96.
[72] 2.11.

Protection Act 1998 for the electronic storage of data were adhered to at all times.[73] The author wrestled with whether to include a methodological appendix to this thesis containing the raw data obtained, as is common in studies of this kind. Ultimately, the decision was taken not to do so. It was thought that to do otherwise may potentially prejudice those directors whose disqualifications had lapsed (or would eventually lapse). Naturally, redaction of the data was considered as an alternative. However, it was concluded that doing so, in a way that would be adequate to protect individual identities, would render the information largely meaningless in any case.

1.17 It is noteworthy that in the initial planning stages of this thesis a form of primary research, in the form of a questionnaire sent to all disqualified directors, similar to Hicks' study, was considered.[74] This idea was ultimately abandoned, partly on financial grounds, but predominantly due to the potential for ethical issues to rapidly spiral out of control. The very last thing that the author would have wanted would be to create any impression that he was 'hounding' those who had (in some cases at least) already suffered enough: the loss of their entrepreneurial freedoms; in many cases bankruptcy; and all that stems from those things: deterioration of relationships, the loss of family homes and so forth. The potential repercussions, it was thought, outweighed the benefits of the approach. As will be suggested in the concluding chapter of this thesis,[75] however, the lack of primary research evaluating the attitudes of directors to the enforcement regime overall provides an opportunity for further empirical engagement going forward.

---

[73] Information Commissioners Office, 'Data Protection Principles' available at <http://bit.ly/1E2lQ8V> accessed 10 July 2017.
[74] Hicks (n 18).
[75] ch 7

Structure of the Thesis

1.18 Following this introductory chapter, designated Part I, Part II will deal with public enforcement; namely directors' disqualification. The first of the two chapters in this Part, Chapter 2, will pursue a doctrinal analysis of the effectiveness of disqualification. Chapter 3, however, will introduce the reader to the author's empirical study of disqualification undertakings as a means of augmenting and verifying the findings of its predecessor chapter. Part III, again comprising two chapters, will deal with private enforcement. Chapter 4 will deal with the substantive areas of wrongful and fraudulent trading. Chapter 5 will focus on the new power of an insolvency officeholder to assign *inter alia*, wrongful and fraudulent trading claims, pursuant to the SBEEA 2015, and explore the impact that this recent development may have in terms of the effectiveness of those mechanisms for the future. The improper trading mechanisms, although distinct, are linked together in this thesis due to the similarities between the two in terms of the analysis undertaken. To separate the mechanisms, it was determined, was structurally unworkable as it would have required repetition or substantial cross-referencing. Part IV, finally, will deal with reforms and concluding remarks. In the penultimate chapter, Chapter 6, the author will return to many of the basic concepts set out in this introductory chapter. In particular, as has been set out, the need for the regulatory devices discussed within this thesis arises from the nature of access to limited liability as being both free and uncontrolled. As will be demonstrated throughout the course of this thesis, the simplicity with which limited liability can be accessed, when coupled with the *ex post facto* operation of the legal mechanisms available to hold delinquent managers to account is in fact something of a poisonous brew. The author therefore, in that chapter, suggests how more wide-reaching, fundamental, reform might be achieved and implemented by tackling that issue at source thereby obviating (or at least reducing) the need for reliance on *ex post facto* enforcement. Ultimately, this will lead to some final considerations, in Chapter 7, the concluding chapter of this thesis, as to the current state of enforcement regime in its totality, its overall success or failure, and thoughts for the future.

1.19 Given the way in which effectiveness is to be measured each chapter in Parts II and III will begin with a brief introduction to the mechanism in question. This will provide a platform for further analysis of the underlying rationale, aims and objectives against which the mechanism will then be judged. The exception to this rule is Chapter 5, given that these matters will are dealt with in the previous chapter. Each of these chapters will then go on to assess the operation of the particular mechanism with a view to determining its effectiveness. As each chapter proceeds, the author will also set out suggestions as to potential reforms, specific to that mechanism, that may aid in improving its effectiveness. These reforms are distinct from those set out in Chapter 6, which are more universal.

1.20 It is of note, perhaps contrary to the traditional approach of thesis construction, that each chapter operates more or less as a standalone entity; albeit each is focussed sharply on the underlying research question. This approach was taken due to the significant amount of ground that is covered. The thesis covers three distinct mechanisms, each of which suffers its own difficulties, though operates largely independently of the others. As such, as has been explained, it is Part IV which ultimately draws all of this together in order that the reader may appreciate the successes and failures of the enforcement regime in a more holistic way.

1.21 With that said, the thesis now turns to deal with director disqualification.

Part II

PUBLIC ENFORCEMENT

2

DIRECTORS' DISQUALIFICATION

2.1 The next two consecutive chapters will consider the main public enforcement mechanism, i.e. directors' disqualification. As distinct from the private mechanisms discussed later in this thesis, those pursued for disqualification are investigated and prosecuted by the IS, on behalf of the SS for DBEIS. It should be remembered however that the public and private enforcement mechanisms are not mutually exclusive. It may indeed be quite proper in the circumstances for a liquidator to take action against a director, whilst the same individual is simultaneously being investigated by the IS for possible disqualification.[76] This chapter and the next will explore the effectiveness of disqualification. They will do so first, in this chapter, with a doctrinal analysis of how disqualification operates. This will uncover some of the inherent difficulties associated with the regime, and assess its effectiveness as against its underlying rationale and objectives. The second chapter will assess disqualification through the lens of reality by way of an empirical study. Through the analysis of both theoretical and practical

[76] Indeed, with the implementation of compensation orders and undertakings, dealt with later in this chapter, the interaction between the two is likely to become all the more noticeable, if not strained. See: 2.34.

elements, a more well-rounded understanding of disqualification thus emerges. The chapter first turns to a terse exposition of the essential provisions.

DISQUALIFICATION PROPER: THE ESSENTIAL PROVISIONS

2.2 The phrase 'disqualification proper' when used in this thesis refers to either a disqualification order or undertaking having the effect set out in section 1 or 1A of the CDDA 1986. In the interests of brevity, and given the extent of the analysis to be undertaken, a substantive exposition of the law on disqualification is unwarranted. Such matters are more than adequately covered elsewhere.[77] Though, for convenience, the author will set out the bare minimum detail necessary to an understanding of the ensuing analysis. Under the CDDA 1986 a court is empowered in various circumstances to make a disqualification order against an individual, or she may herself give an undertaking to the SS so as to avoid court proceedings. The maximum period of disqualification is 15 years. Disqualification undertakings, which have precisely the same legal status as a court order, were introduced by the IA 2000 in 2001.[78] The SS has three years from the relevant date of insolvency to accept an undertaking or make an application to the court for a disqualification order.[79] It is important to note that, formerly, this limitation period was *two* years. It was however recently increased (alongside other changes in this area)

[77] For instance, Adrian Walters and Malcolm Davis-White, *Directors' Disqualification & Insolvency Restrictions* (3rd edn, Sweet & Maxwell 2010).
[78] For a detailed exposition of the history of the legislation, leading up to undertakings see: Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) ch 1.
[79] CDDA 1986, s 7(2).

by the SBEEA 2015,[80] for reasons to be dealt with in due course.[81] Sections 1 and 1A mandate that where disqualified, whether by order or undertaking, a person:[82]

(a) will not be a director of a company, act as receiver of a company's property or in any way, whether directly or indirectly, be concerned or take part in the promotion, formation or management of a company unless (in each case) he has the leave of a court,[83] and;

(b) will not act as an insolvency practitioner.[84]

2.3 A 'director' is defined by the CDDA 1986 as including, of course, *de jure* directors; but also *de facto* and shadow directors.[85] One of the oddities of directors' disqualification is that it can arise in a number of different circumstances, including in both criminal and civil proceedings. It should be noted at the outset that although other types of disqualification exist[86] the dominant focus here will be on directors that are disqualified under section 6 of the CDDA 1986, set out below, where they are deemed to be 'unfit'. The primary reason for this is that the proceedings under this section account for some 94.5 per cent of disqualifications on average.[87] In so far as is relevant section 6 reads as follows:

---

[80] SBEEA 2015, s 108(1).
[81] 2.25-26.
[82] Section 1 pertains to court orders; section 1A to undertakings. Though, the wording is replicated across both sections.
[83] As to the meaning of 'without leave of the court' see CDDA 1986, s 17 which permits a director to make an application for leave to act in the management of a company, notwithstanding her disqualification. See also David Milman, 'Partial disqualification orders' (1991) 12 Co Law 224; Alice Belcher, 'What makes a director fit? An analysis of the workings of section 17 of the Company Directors Disqualification Act 1986' (2012) Edin LR 386.
[84] As an aside, disqualified persons may come under a moral obligation to disclose the fact that they are disqualified, for instance, to professional regulators or employers; on threat of sanction.
[85] CDDA, ss 22(4) and 22(5).
[86] Including disqualification for wrongful or fraudulent trading pursuant to CDDA 1986, s 10, dealt with later in this thesis: 4.10.
[87] IS, *Insolvency Service Enforcement Outcomes 2016-17* (2017) <http://bit.ly/2u35zoP> accessed 1 July 2017, Table 1A.

6 Duty of court to disqualify unfit directors of insolvent companies

(1) The court shall make a disqualification order against a person in any case where, on an application under this section, it is satisfied –

(a) That he is or has been a director of a company which has at any time become insolvent (whether while he was a director or subsequently), and

(b) That his conduct as a director of that company (either taken alone or taken together with his conduct as a director of one or more other companies or overseas companies) makes him unfit to be concerned in the management of company…

(4) Under this section the minimum period of disqualification is 2 years, and the maximum period is 15 years.

2.4 Section 6 only deals with court orders. It is section 7 that empowers the SS to accept undertakings, where it is 'expedient in the public interest' to do so and the criteria under section 6(1) is fulfilled. However, for convenience, the author will refer to 'section 6 proceedings' when dealing with both orders and undertakings throughout this thesis. There are a few matters worthy of initial note. Unlike other types of disqualification, section 6 only applies to *insolvent* companies. Moreover, the title of the section notes the '*duty*' of the court to disqualify an individual. This is because, again unlike most other types of disqualification, once the requisite 'unfitness' criteria has been met, the court *must* disqualify the individual concerned for a period of at least two years, subject to the 15-year maximum period. The implications of mandatory disqualification[88] and, importantly, the meaning of 'unfitness' itself[89] will be subject to substantive exposition below when considering the effectiveness of the regime.

[88] 2.6.
[89] 2.28.

OBJECTIVES AND RATIONALE

2.5 Analysis of debate during the passage of the CDDA 1986 through Parliament and subsequent judicial comment permit the objectives of disqualification to be distilled into three main points:[90]

(a) the protection of the public from abuses of limited liability;[91]

(b) deterring directorial misconduct;[92] and

(c) the encouragement of probity in corporate management.[93]

Given the banning effect of disqualification, the need to strike a proper balance between the right of an individual to be enterprising on the one hand, and prevention of abuse of limited liability on the other, is more acute than perhaps it is in the case of the private mechanisms discussed later in this thesis. Getting the balance right, it is argued, is crucial to a successful regime. A regime that is too lax will inevitably lead to a lack of protection for the public, and weak deterrence. A regime at the other extreme may instead become too inhibitive on individual freedoms, thereby stifling enterprise. Each objective will therefore be discussed in turn at this point, so that some general arguments can be made relation to how (if at all) successfully they are fulfilled. The discussion will then turn to more specific issues that potentially have a bearing on effectiveness.

---

[90] Helpfully listed at: NAO, *Report by the Comptroller and Auditor General: The Insolvency Service Executive Agency, Company Director Disqualification* (HC 1992-1993, 907) para 1.4.

[91] See, for example, *Secretary of State for Trade and Industry v Tjolle* [1998] BCC 282, 284; Walters and Davis-White (n 77) 2-04; Cork Report (n 68) para 1808; *Re Polly Peck International (No 2)* [1993] BCC 890, 896; *Re Cladrose Ltd* [1990] BCC 11, 18.

[92] Walters and Davis-White (n 77) 2-19; *Re Westmid Packing Services Ltd* [1998] 2 All ER 124, 131-2.

[93] *Re Blackspur Group Plc (No 2)* [1998] BCC 11, 15; *Re Atlantic Computers Plc,* June 15 1998, Ch D (unreported); *Re Barings Plc (No 5)* [1999] 1 BCLC 433. See also *Re Swift 736 Ltd* [1993] BCC 312, 315: '[l]imited liability is a valuable tool in the promotion of trade and business, but it must not be misused…[disqualification]…is an important sanction introduced by Parliament to raise standards in this regard' (Sir Donald Nicholls VC).

Protection of the Public

2.6 *Punishment vs. Protection* The state has generally been unwavering in stating that the protection of the public is the primary aim of disqualification.[94] Judicial and academic comment, however, has historically been far less clear. Dine and Finch, in particular, have been highly critical of whether the current approach truly embodies protectionist principles. Dine has suggested that disqualification actually concerns the application of penal or quasi-penal rules in what is a criminal or quasi-criminal process, albeit by the civil courts.[95] If disqualification proceedings are inherently 'criminal' in nature, rather than regulatory, she argues, directors should be investigated, prosecuted and adjudicated upon in the normal way in the criminal courts.[96] This is more than an issue of semantics: to masquerade criminal proceedings as civil regulatory ones has the effect of depriving defendants of the full complement of rights available to them in a criminal trial, as well as the higher standard of proof. Indeed, as Hicks alludes to, and as is reiterated here, should the higher criminal standard ever be imposed in disqualification cases the onerous burden of proof on the prosecution would likely be very difficult indeed to overcome in most cases.[97] There is therefore, it must be recognised, some motive (albeit an underhand one) for the State to retain the *status quo*. Finch has suggested that the desirability of either a punitive or protectionist approach is dependent on whether access to limited liability is to be viewed as a privilege or an

[94] Walters and Davis-White (n 77) 2-04.
[95] Janet Dine, 'Punishing directors' (1994) JBL 325.
[96] ibid, 336-337.
[97] Andrew Hicks, 'Director disqualification: can it deliver?' (2001) JBL 433, 454.

employment right.[98] If viewed as an employment right, as appears to be Finch's position, then the only means of removing it ought to be through criminal proceedings.[99] Mere privileges, however, she argues, can legitimately be removed on the balance of probabilities through a regulatory framework as at present.[100] In the context of this thesis, however, the *desirability* of either a protectionist or punitive system is of limited relevance. That notwithstanding, it ought to be said at this juncture that if the view is taken that directors *ought* to be punished, then the correct approach must be to revisit potential criminal sanctions for directors rather than to simply muddle through with the current system. Research in this area by Von Hirsch and Wasik, however, seems to indicate that as a penal sanction director disqualifications are practically unworkable in any event,[101] though such matters are strictly beyond the remit of this thesis. The central question to be explored here is whether the regime is, in fact, aligned with protectionist principles. Because, in this work, adherence to the objectives laid down by Parliament are considered the yardstick by which effectiveness can be measured. It may be that a punitive regime is desirable, however, that is not the approach Parliament has chosen. Therefore, put simply, a regime seeking to *punish* errant directors for their wrongdoing does not accord with the objectives of disqualification, and is therefore not fit for purpose. The real concern for discussion here, it is submitted, lies in if the regime

[98] Vanessa Finch, 'Disqualifying Directors: Issues of Rights, Privileges and Employment' (1993) 22(1) ILJ 35; See also Vanessa Finch, 'Disqualification of Directors: A Plea for Competence' (1990) 53 MLR 385.
[99] Finch, 'Disqualifying Directors: Issues of Rights, Privileges and Employment' (n 98) 36.
[100] ibid 36-37.
[101] Antrew Von Hirsch and Martin Wasik, 'Civil Disqualifications Attending Conviction: A Suggested Conceptual Framework' (1997) 56(3) CLJ 599, 618-619 as quoted in Katharina Möser, 'Restrictions after personal insolvency' (2013) JBL 679, 687. Möser, at 687, suggests that disqualification 'lack[s] the even-handedness that is required of a criminal sanction…[as] the actual impact of a disqualification on the concerned individual typically depends very much on his personal circumstances'.

transpires to be punitive in practice, despite being dressed up by the State in the clothing of protectionism. This concern is magnified should it be the underhanded intention of the State to take this approach; perhaps in order to circumvent the defendant's rights in a criminal trial, or take advantage of the lower standard of proof required so as to bolster the number of disqualifications achieved.[102]

2.7 It is argued here that whether the regime is considered punitive is largely a matter of perception. First, the two objectives – punishment and protection – are not necessarily mutually exclusive. Even if the courts and the SS have the best of intentions in pursuing solely a protectionist agenda as Parliament intended, there may be resulting consequences that are, or are perceived as being, punitive. Indeed, it is hard to imagine that, if surveyed, the majority of disqualified directors would not consider (at the very least) some part of the process as being punitive. It is after all a very serious matter: particularly for the professional director, where a period of disqualification can have life changing consequences. The State itself has recently recognised the 'serious punitive and financial effect'[103] of disqualification on the individual. And, whilst there have undoubtedly been a number of judicial decisions that have been couched in punitive terms,[104] equally there have been others that take a protectionist approach.[105] It

[102] Which is desirable from the perspective of the state, given that a greater number of disqualifications is often marketed as being indicative of a successful regime.
[103] T&T Discussion Paper (n 14) 10.3. Moreover, disqualification was recently labelled a 'punishment' by the DBEIS Select Committee: DBEIS Committee, *Corporate governance: Third report of session 2016-17* (HC 2016-17, 702) para 36.
[104] Some of the decisions that have potentially punitive undertones include: *Re Cladrose* (1990) BCC 11; *Re Swift 736 Ltd* (1992) BCC 93; *Re Dominion International Group Plc* [1995] 1 WLR 649; *Re C U Fittings Ltd* (1989) 5 BCC 210; *Secretary of State for Trade and Industry v Hickling* [1996] BCC 678.
[105] See generally: Finch, 'Disqualification of Directors: A Plea for Competence' (n 98); Also Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) 2.37-2.38. The author notes that the vast majority of decisions, particularly later ones, adopt a protectionist approach: *Re*

appears to have been the decisions in the former category that has led to commentary from those such as Dine. Given that the period of disqualification to be imposed is, in effect, a sentencing exercise[106] it is hard to dispute that disqualification has a number of 'criminal' elements to it. However, as Williams states:

> The strict question of whether disqualification 'is' a protective or a punitive sanction is…neither here nor there (and is clearly arguable either way). What is clearly more important is…does the sanction, both generally and in individual cases, provide effective protection for the public?[107]

Thus, in line with that argument, if a disqualification is imposed with the intention of protecting the public (despite potentially punitive repercussions), then the underlying purpose must be considered as fulfilled. It is only in circumstances where either the strict intention is expressed as being to punish the individual in question, *or* where the disqualification is imposed in a way that is so manifestly excessive so as to go beyond protection, that the primary objective of disqualification can be said to have been frustrated. In relation to the second circumstance, *Re Cladrose Ltd*[108] has been cited by Finch as an example of evidence of the punitive nature of the current regime.[109] In that case, before Harman J, one of the two directors to be disqualified was a chartered accountant. The professionally qualified director, said the learned judge, was more culpable than his unqualified colleague for the company's failure to file statutory

---

Ipcon Fashions Ltd (1989) 5 BCC 773; *Re Crestjoy Products Ltd* [1990] BCC 23; *Re Sevenoaks Stationers (Retailer) Ltd* [1990] BCC 765 (CA); *Re Southbourne Sheet Metal Co Ltd* [1993] WLR 244 (CA); *Re Polly Peck International Plc* [1993] BCC 890; *Re Pamstock Ltd* [1994] BCC 264; *Secretary of State for Trade and Industry v Bannister* [1995] BCC 1027; *Secretary of State for Trade and Industry v Jeffrey Albert Vane* Ch. D (Companies Court) (30 June 1997) [1997] WL 1104724; *R v Edwards* [1998] 2 Cr App R (S) 213; *Re Blackspur Group Plc (No. 2)* [1998] BCC 11 (CA); *Re Westmid Packing Services Ltd* [1998] BCC 836; *R v Evans* [2000] BCC 901 (CA); *Official Receiver v Stern* [2000] WLR 2230 (CA); *Re Cedarwood Productions Ltd* [2004] BCC 65 (CA); *Secretary of State for Business, Innovation and Skills v Brandon Weston, Christopher David Williams* [2014] EWHC 2933 (Ch); *Re Pantmaenog Timber Co Ltd* [2004] 1 AC 158.

[106] *Re Westmid Packing Services Ltd* [1998] BCC 836, 843.

[107] Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) 2.38.

[108] [1990] BCC 11

[109] Finch, 'Disqualification of Directors: A Plea for Competence' (n 98) 388.

accounts and returns. As such, he was disqualified for a longer period. However, the discussion becomes somewhat circular as, to return to Williams' point, it can be argued either way; given that it is largely a matter of perception. For example, it may equally be said that a professional person ought to be disqualified for a longer period of time in order to sufficiently protect the public as incompetent, negligent, or dishonest qualified persons can potentially exact more damage than their unqualified counterparts. Even if the view is taken that such cases demonstrate a penal approach, it is not to say that disqualification is *fundamentally* penal. The better view, it is submitted, is that those are merely wrong decisions. In any event, recent judicial authority seems to suggest a distancing from punitive terminologies, leaving the author the query whether this rhetoric is now a thing of the past.[110]

2.8 However, given the recent introduction of compensation orders and undertakings to the disqualification arena, there is potential for this argument to once again rear its head. The court can now order, or the SS can seek an undertaking from, a disqualified director to pay compensation; either as a contribution to the assets of the company, or directly to individual creditors.[111] It is therefore submitted that this is one area to be mindful of for future discussion. Though, the author's view is that the argument remains the same. There is nothing 'fundamentally penal'[112] about awarding compensation to creditors for the loss caused by misconduct (though of course financial punishment may be a by-product of it). To the contrary, this provision has considerable

---

[110] *Secretary of State for Business, Innovation and Skills v Brandon West, David Christopher Williams* [2014] EWHC 2933 (Ch) at [41].
[111] CDDA 1986, s 15A.
[112] Similar sentiments were expressed by Browne-Wilkinson VC about disqualification proper: *Re Lo-Line Electric Motors Ltd* (1988) 4 BCC 415, 419.

potential to reinvigorate the direct protection benefit for creditors (i.e. the 'public') by compensating them for any losses incurred. However, it is submitted that the approach of the courts and the SS must continue to be focused towards protectionism if the underlying purpose of disqualification is to be achieved. A director who has to compensate creditors over and above the losses actually incurred, or who is ordered to pay a form of aggravated or punitive damages would have, in this author's mind, a legitimate argument that the decision was made without regard for the underlying objective of the regime. This does not, however, seem to be how the regime is intended to operate.[113] Thus, it is submitted, a director who is simply ordered to pay back what he 'owes' ought to be afforded little scope for such complaint.

2.9 *Protection from what?* Disqualification is generally held out as being to protect the public specifically from those who 'abuse limited liability'.[114] Limited liability and disqualification are therefore inextricably linked.[115] This being the primary aim, it ought to follow logically, then, that a disqualified person should still be able to set up in business so long as she trades in an *unlimited* form. Surprisingly, this is not the case. Within the terms of the CDDA 1986, a disqualified person is barred from being involved in the promotion, formation or management of a 'company'. The term 'company' is defined within section 22(2) as meaning:

(a) a company registered under the Companies Act 2006 in Great Britain, or

---

[113] This is stated on the basis that the section requires there to be a nexus between the loss to creditors and the misconduct for liability to attach.
[114] See for instance, to name but a few authorities: *Re Sevenoaks Stationers (Retail) Ltd* [1990] BCC 765 (CA), 763; *Re Stanford Services Ltd* (1987) 3 BCC 326, 336; *Re Douglas Construction Services Ltd* (1988) 4 BCC 553, 557; *Re Cladrose* [1990] BCC 11, 18; The NAO has stated disqualification is designed to 'protect the public and commercial world from those who abuse limited liability': NAO Follow-Up Report (n 15) 1.
[115] ch 1.

> (b) a company that may be wound up under Part 5 of the Insolvency Act 1986 (unregistered companies)

This definition is therefore broad enough to extend the banning effect of disqualification beyond the limited company. It would also include unlimited liability companies and companies limited by guarantee; both of which are incorporated under the CA 2006.[116] If disqualification is held out as being to protect the public specifically against abuses of limited liability, then the wording of the CDDA 1986 is evidently at odds with that rationale. To avoid this contradiction, it must be assumed that disqualification serves a broader purpose. It might be described more generally as being to 'protect the public' from misconduct arising out of the conduct of corporate affairs. However, why the line is drawn in this particular way is unclear. It seems strange that a disqualified person can carry on business the very next day as a sole trader, perhaps even building it to a large empire,[117] yet cannot do so using an incorporated vehicle even on terms of unlimited liability. Indeed, in *Re Dawes and Henderson (Agencies) Ltd*[118] Sir Richard Scott VC, granted an application for section 17 CDDA 1986 leave to direct an unlimited company, on that basis.[119] This decision, it is argued, embodies the notion that disqualification is primarily to protect from the abuse of limited liability; not merely just poor trading practices generally. Therefore, although a disqualified director can rely on the section 17 CDDA 1986 process to obtain leave, it is argued that the better solution, to accord

---

[116] There are also other miscellaneous entity types caught by the definition including building societies, incorporated friendly societies, NHS foundation trusts and open-ended investment companies. See CDDA 1986, ss 22A-D.

[117] Although the soletradership is often associated with small companies, this is not always the case. Mike Ashley, founder of the sports retailer *Sports Direct,* initially traded (though as *Mike Ashley Sports*) as a sole trader; building an empire of 100 stores before the switch to a limited company was made. See the Wikipedia entry for 'Mike Ashley (businessman)' at <http://bit.ly/2vHxEiU> accessed 1 January 2016.

[118] [2000] BCC 204

[119] *Re Dawes and Henderson (Agencies) Ltd* [2000] BCC 204, 212.

with its objectives, would instead be to limit the effect of disqualification solely to *limited* companies.

2.10 *Protection for whom?* The phrase 'protection of the public' is in itself rather illusory. In the natural sense of the word, 'public' is one which encompasses the whole of a population or society. Protection is therefore a measure justified as being utilitarian in nature, i.e. for the greater good of the populous as a whole. It is incontrovertible that where limited liability is abused, leading to insolvency, it can cause great losses to the community at large. It is important to note, therefore, that it is not just creditors that need to be protected. For example, the NAO have expressed the role of disqualification as being to protect the 'commercial world'[120] more generally. Moreover, Walters and Davis-White posit analysis of the implications of disqualification for shareholders, investors, consumers and employees.[121] It is argued here that although the protection of those stakeholders is no doubt important in the context of promoting public confidence in the regulatory aspect of corporate culture in the UK they are often incidental to disqualification cases. The main focus as seen throughout the case law is the protection of both the public and private creditor.[122] The need to protect creditors from unfit directors is vital, though, to take a step back, it must be recognised that most creditors *do* in fact get paid.[123] However, as disqualification occurs after the fact it is of course merely a mechanism of future damage limitation. Disqualification proper is therefore unlikely to provide great comfort to affected creditors. After all, creditors do not

[120] NAO Follow-Up Report (n 15) 1.
[121] Walters and Davis-White (n 77) 2-15 – 2-22.
[122] 3.13.
[123] Prentice (n 26) 99.

necessarily care about *why* they have not been paid, simply that they *have not* been paid. This is of course an inescapable weakness of *ex post facto* regulation.

Deterrence

2.11 It is fair to say that although it is often held out as being a core aspect of the regime by the State, the deterrence effect of the disqualification regime is, in reality, rather weak.[124] Deterrence, it being pervasive, will be revisited throughout this chapter when dealing with the substantive issues. However, at this juncture, it is worth setting out some of the key areas of concern. The potential impact of a *successful* deterrence agenda should not be overstated. This is because deterrence can be a powerful motivator to alter behaviour. To operate successfully, however, it is argued four primary factors must be present: firstly, directors must be aware of disqualification itself to be deterred; secondly, they must be aware of the sanctions that they may face; thirdly, they must understand the acts or omissions that may lead to being sanctioned; and finally, the sanctions themselves must have sufficient 'teeth' in order to be heeded, so as to stimulate a change in behaviour. If these factors are not present, there will be no deterrence or, at best, very weak deterrence.

[124] According to the NAO, of those that were aware of the CDDA 63 per cent considered it had little or no relevance to their business; and 90 per cent thought it had no impact on them personally: NAO, *Report by the Comptroller and Auditor General: The Insolvency Service Executive Agency, Company Director Disqualification* (HC 1992-1993, 907), para 4.3 (NAO Report); In the NAO Follow-Up Report (n 15) para 3.33, 64 per cent of those surveyed thought disqualification was unsuccessful in deterring unfit conduct; Also see Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 10.

2.12 *Awareness* Awareness of disqualification is undoubtedly very low.[125] This is perhaps the greatest stumbling block at present to creating an effective deterrent. Moreover, little has changed in this regard since the genesis of disqualification. As stated previously, it is impossible to deter, and therefore foster a change in the behaviour of, directors who are simply unaware of the consequences they may face. In the two reports published by the NAO, 58 per cent[126] and 66 per cent[127] of directors that were surveyed, respectively, stated they were unaware of disqualification as a sanction. Even 57 per cent of the directors of those who knew about the CDDA 1986 said they were 'not well informed' about disqualification procedures.[128] In Hicks' survey, 76 per cent of those surveyed thought disqualification should be better publicised.[129] As Williams notes, a 2009 IS *Stakeholder Satisfaction Survey* suggests the position has not changed since that time. He records that 42 per cent of those surveyed thought that sanctions (including disqualification) were 'quite effective' or 'very effective' at deterring wrongdoing.[130] This author notes that a more recent 2012 IS *Stakeholder Confidence Survey* showed that only 43 per cent of directors surveyed were aware of disqualification as a sanction,[131] broadly at similar levels as in 2011.[132] It is especially

[125] See the empirical work conducted by Hicks, ibid 10 and the NAO: NAO Follow-Up Report, para 3.33. See generally: Richard Williams, 'Civil Recovery from Delinquent Directors' (2015) 15(2) JCLS 311, 335.
[126] NAO Report, para 4.3.
[127] NAO Follow-Up Report, para 2.49.
[128] NAO Report, para 4.3.
[129] Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 10.
[130] See IS, *Business Confidence Stakeholder Satisfaction Survey 2009: Management Summary* (2009), Table 6 as noted in Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 2.70. The URL provided by Williams was unavailable at the time of writing and no alternative source could be located, thus it is not repeated here. By way of limitation it should be noted that the sanctions in this survey including others beyond disqualification, so it cannot be entirely relied upon in assessing awareness.
[131] IS, *Stakeholder Confidence Survey 2012* (2013) available at <http://bit.ly/2iJGZEL> accessed 1 April 2017, Table 5.2.
[132] ibid, Table 5.1.

worthwhile to set out that the latest *Stakeholder Confidence Survey* available at the time of writing, which boasts an overall 91 per cent awareness rating[133] *did not survey directors* unlike its predecessor surveys (or at least the results were not published). Evidently, merely being selective as to the statistics deployed does little more than brush the issue under the carpet; further deepening the issue. It goes without saying: this is particularly troubling.

2.13 Thus the IS, and the state more broadly, should they wish to increase the effectiveness of this objective, need to undertake a more widespread campaign to dramatically improve awareness. Current efforts in this regard are either lacklustre, improperly targeted or both. Respondents of the 2012 *Stakeholder Confidence Survey* suggested several methods for increasing the profile of disqualification, including the compulsory education of directors, or 'naming and shaming' those disqualified in local and national press, as a matter of course.[134] The former suggestion will be discussed in some depth in the penultimate chapter of this thesis.[135] As to the latter, the implication is that the practice at that time was only to report the most 'exciting' or topical cases. However, in recent times the IS have attempted to improve the situation somewhat by the use of social media platforms, such as Twitter. But, as might be expected, the author notes that many of the IS's 'followers' are insolvency professionals, large organisations and academics. It rather goes without saying that the reach of the IS, without more proactive measures to target directors specifically, is thus likely to be limited to persons

[133]IS, *Stakeholder Confidence Research: Executive Summary 2015-2016* (2016) available at <http://bit.ly/2eschi1> accessed 1 April 2017, Table 3.3.1.
[134] IS, *Stakeholder Confidence Survey 2012* (n 131) 49-51.
[135] ch 6.

who are already intimately familiar with disqualification. Nonetheless, efforts to improve awareness in this fashion must of course be welcomed. However, the 2012 *Stakeholder Confidence Survey* previously mentioned paints a rather bleak picture in this regard: only 4 per cent of directors surveyed were aware of enforcement related communications.[136]

2.14 *Enforcement generally and dishonest directors* Some people may simply be incapable of being deterred, i.e. those who deliberately set out to abuse limited liability.[137] Thus, in the case of this individual, the objective is not fulfilled and, as Hicks notes, although it restricts their business activities, disqualification proper provides limited recourse.[138] It is suggested that a person who purposefully rips off creditors is less likely to be deterred from doing so if the ill-gotten gains potentially outweigh the benefits. Non-compliance, from the perspective of the errant director, may be both rational and financially desirable.[139] Just under half of the directors in Hicks' survey said they were unaware of the sanctions available if they were caught being in breach of a disqualification order.[140] Moreover, some 39 per cent thought that the likelihood of being caught acting in contravention of one was low.[141] A general point stemming from this discussion is that even for the vast majority of directors who do not set out to deliberately abuse limited liability, the deterrence objective is unlikely to be fulfilled should the threat of sanctions (i.e. disqualification) be perceived as weak. In Hicks'

[136] IS, *Stakeholder Confidence Survey 2012* (n 131) 8.
[137] Many of these arguments are revisited, and further expanded upon in the penultimate chapter when dealing with the potential target audience of education and training for directors.
[138] Andrew Hicks, 'Director disqualification: can it deliver?' [2001] JBL 433, 440.
[139] See, for more detail, Richard Williams, 'Disqualifying Directors: A Remedy Worse than the Disease?' (2007) 7(2) JCLS 213, 235-236.
[140] Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 10.
[141] ibid.

research, 60 per cent of those surveyed suggested that their knowledge of disqualification had no impact on how they ran their ailing company.[142] This broadly accords with the NAO's research, which set out that 63 per cent of those surveyed considered disqualification had little or no relevance to their business; and 90 per cent thought it had no impact on them personally.[143] More recently, the 2012 *Stakeholder Confidence Survey* found that only 37 per cent thought that disqualification was an effective deterrent to misconduct generally.[144]

2.15 *Owner-managers and disqualification* Owner-managers of small concerns, it is submitted, are far less likely to be deterred than *professional* directors. This is for two reasons. First, as Hicks recognises, these individuals will invariably be heavily invested (both emotionally and financially) in their business.[145] As such, 'disqualification may not be a sufficient sanction to induce them to behave better when faced with the possible failure of their business'.[146] Put simply, these individuals are far more likely to try and trade out of insolvency in order to save the business and thus may not be deterred with the threat of sanctions. Secondly, these individuals do not have very far to fall.[147] Unlike the professional director, they can simply set up in business the next day – albeit as a sole trader. Though, as is argued in the penultimate chapter, the soletradership (or other form of unlimited liability vehicle) may indeed be the more appropriate vehicle for business for such individuals.[148] Thus, the author is sceptical as to whether owner-

[142] ibid 126.
[143] NAO Report (n 124) para. 4.3.
[144] IS, *Stakeholder Confidence Survey 2012* (n 131) Table 5.4.
[145] Hicks, 'Director disqualification: can it deliver?' (n 138) 441.
[146] ibid 441.
[147] ibid 441-442.
[148] ch 6.

managers can really ever be deterred. These factors may well go some way towards explaining why owner-managers make up the vast majority of disqualifications.[149] Or, vice-versa, why the deterrence effect is so poorly felt. It is submitted this must, notwithstanding the other issues identified, be evidence of a failure of the deterrence objective in and of itself.

2.16 *Deterrence post-disqualification* This is a matter that will be revisited in more depth in the penultimate chapter, when discussing general reforms to the enforcement regime.[150] The central point is this. Even after a director is disqualified, what about when that disqualification lapses? There is a continuing need to ensure deterrence, after the fact, so that a director is not tempted to reoffend should she return to the market. On the contrary, the current regime seems to treat disqualified directors as lost causes; there are no follow-up measures designed to instigate a change in behaviour. It almost appears to be a hope of the state that the process of disqualification in itself is enough to do so. Behavioural change is however crucially important for those few directors that do return to the market. As Loughrey has argued, through having to justify their behaviour in an adversarial context, directors will seek to minimise the degree of their misconduct rather than accepting that it was wrong.[151] Thus, they will avoid altering their behaviour in any future endeavours. Directors need to appreciate the legitimacy and fairness of the process and be supported in any rehabilitation should they so desire it. It is submitted, that only in this way can a change in behaviour be effected. On the contrary, Hicks'

---

[149] See Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 8. But also this author's own empirical research in the next chapter.
[150] ch 6.
[151] Joan Loughrey, 'Smoke and mirrors? Disqualification, accountability and market trust' (2015) 9(1) LFMR 50, 55.

research suggested that a majority of directors surveyed felt victimised as a result of the proceedings taken against them.[152]

Raising Standards of Corporate Management

2.17 As to the final objective, it is closely linked to those addressed previously, namely the specific deterrent of disqualification and its primary aim of protecting the public. The NAO noted in its *Follow-Up Report* that:

> [B]y deterrence and by the promulgation of orders made by the courts, to contribute to fostering the integrity of markets generally and improving the standards of company stewardship in particular, but without inhibiting genuine enterprise and entrepreneurial management.[153]

The statement might now be read as to include the promulgation of disqualification undertakings, and even compensation orders and undertakings.[154] This objective was also advanced by Lord Woolf in *Re Blackspur Group (No. 2)*,[155] who stated that the 'encouragement of higher standards of honesty and diligence in corporate management'[156] is a general deterrent by-product of disqualification. The idea is that as disqualifications are made, this in turn causes a widespread positive effect on corporate governance practices. This in theory has the benefit of protecting the public by reducing misconduct where it might otherwise have occurred but for the deterrent. The real-world impact of this objective is difficult, if not impossible, to measure as Hicks has noted.[157] By reason of the interconnectivity with deterrence, achieving measurable success is thereby, it is argued, limited in this objective in much the same way. For instance, if the

---

[152] Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 123.
[153] NAO Follow-Up Report (n 15) para 1.5.
[154] Given that, of course, the report pre-dated their implementation.
[155] [1998] BCC 11.
[156] *Re Blackspur Group Plc (No 2)* [1998] BCC 11, 15.
[157] Hicks, 'Director disqualification: can it deliver?' (n 138) 441.

impact of the specific deterrent effect of disqualification is negligible, it is difficult to credibly argue that a general deterrent would be any more effective. In relation to this objective, therefore, the author repeats many of the same arguments set out previously. However, there are additional standalone issues that merit specific consideration.

2.18 *Unfit conduct* By definition, raising standards of management requires an awareness (and therefore dissemination) of the types of conduct deemed to be unacceptable, so that behaviour can be changed. As previously explored, awareness of disqualification is low. Thus, it follows that a director is equally likely to be unaware of the type of conduct that might lead to her being disqualified, whether through 'unfitness' or otherwise. It is therefore all but impossible for them to behaviourally alter course without professional intervention. Granted, whilst a layperson may inherently understand, to give an extreme example, that frauds are wrong, the 'nebulous concept'[158] that is unfitness will be shown later in this chapter to be far more technical.[159]

2.19 *Education* It seems to this author that if this is an object of disqualification, then the current means of achieving it are misdirected. Yet, with proper implementation, simply raising standards across the board is likely to be a very powerful means of reducing abuse. This goes back to the demography of disqualification as largely being owner-managers. Granted, some owner-managers will simply have no regard for their responsibilities. Others will carry them out diligently. The vast majority, however, are entrepreneurs concerned more with running their business; not legal formalities. Whilst they may not want to break the law, they may do so inadvertently due to their ignorance

[158] *Re Polly Peck International plc* [1993] BCC 890, 897.
[159] 2.28.

or incompetence. Educating directors as to what the law is, therefore, ought not only to be a very powerful tool to combat this ignorance, and therefore reduce disqualifications, it is something so basic that the lack of its implementation at present is unforgiveable. The problem with current policy, is that government simply waits and hopes that there will be sufficient dissemination and reporting of directorial misbehaviour; causing others to change their ways. A more direct approach is needed. Government ought to take the initiative to educate directors as to such matters *ex ante*. The proper way to improve standards, it is submitted, must be through direct intervention. This will be a central reform considered in considerably more detail in the penultimate chapter of this thesis.[160] It will be argued there that a proper implementation of a regime of education and training of company directors, before they take up office, is likely the only credible means of truly improving standards. At present, it cannot be said with any confidence that this objective is anything more than a theoretical one. This was a point identified by Hicks in 1998,[161] and very little appears to have changed. Moreover, there is no reason to think, at present, that anything will change in the following two decades unless the state commits itself to more radical action.

2.20 *The leaflet* As part of his research the author contacted CH to determine what routine steps are taken to inform directors as to their legal responsibilities and the consequences of misconduct, in order to gauge whether the State takes any proactive measures in helping to fulfil this objective. The author was particularly interested as to whether communications would be made to directors in relation to the (at the time

[160] ch 6.
[161] Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 76.

forthcoming) changes under the SBEEA 2015. CH confirmed that it does not take any such steps, save for one exception. An initial leaflet published by DBIS entitled 'Directors' Duties' is sent to the service address of each new director on appointment.[162] It details, in plain English, the core director duties set out in sections 171-177 of the CA 2006. It is successful in this respect, and clearly a lot of thought has been put in to making it accessible, understandable, and digestible. However, it is a mere two sides of A5, and makes no reference to consequences of breach of duty. There is no mention of the civil liability provision under section 177 CA 2006, let alone any discussion of wrongful or fraudulent trading, or disqualification. The leaflet is accompanied by a letter which details some of the more administrative responsibilities such as filing annual accounts and a return, as well the need to inform CH of any changes in directorships or the registered office address. The letter also directs the reader to a website containing details of the seminars CH runs on director responsibilities.[163] Hicks notes that a similar practice was in place as at the time of his report in 1998.[164] CH, of course, is largely concerned with the filing of documents and other administrative matters. However, as the registrar holding all records of active directors, they are clearly best placed to provide pertinent information directly across a range of topics including disqualification. Government's failure to mandate that it does so is therefore an obvious and alarming omission, demonstrative of little inclination towards raising standards of management. The letter and leaflet appears to represent the totality of communications that directors receive in relation to their duties, save for those that seek out additional

---

[162] No other steps are taken however.

[163] See CH, 'Events Calendar' available at <http://bit.ly/2wV6SYu> accessed 20 February 2017.

[164] Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 76.

information on the CH or IS websites, or through private training.[165] To return to deterrence, it is therefore unsurprising that awareness is as low as it is thought to be given that no real proactive steps are taken. There may be an element of not wanting to 'burst the bubble' of entrepreneurial spirit in lecturing new appointees with swathes of material on what might be considered by the population at large to be rather tedious matters, much of which is likely to go unread in any case. However, that is rather an unsatisfactory position. Whilst many new appointees may have some loose idea that they are subject to various duties, it cannot be said that the current approach is anywhere near adequate, so as to have the effect of raising standards.

ADMINISTRATIVE DIFFICULTIES

Early Criticisms

2.21 Much of the focus on its effectiveness in the literature has, in fact, revolved around *administrative* concerns. With that said, this section of the chapter turns to explore some of these difficulties before continuing on to deal with some more substantive issues. The effectiveness of the disqualification regime first came under real scrutiny in a series of reports published by the PAC and the NAO. The report published by the PAC, in the 1993-1994 session,[166] examined the administrative efficacy of the disqualification regime and found gross systematic failures. The IS was severely criticised for its methods in managing disqualification cases, with a primary allegation being that it simply took them too long to obtain a disqualification order against an

[165] There are of course numerous books on the topic aimed specifically at directors. For instance, see David Impey and Nicholas Montague, *Running a Limited Company* (Jordans 1990). One of the other problems is that these resources become very quickly out of date.
[166] PAC, 18th Report (HC 1993-1994, 167).

individual.[167] It identified that reports of unfit conduct from IPs, dealt with below, were of a poor quality and, in any case, only 1 out of every 22 reports where unfit conduct was found were actually referred to the IS for investigation.[168] The NAO published two separate reports dealing with the effectiveness of disqualification. The first,[169] in the 1992-1993 session, also uncovered similar matters relating to the poor quality of some reports[170] and, when looking at cases rejected for prosecution by the IS in 1991-1992, uncovered that 29 per cent of these were rejected on the basis that there was not enough time remaining within the (then) two-year statutory limitation period to 'resolve outstanding points'[171], i.e. they were not being dealt with quickly enough. In fact, the NAO observed in most cases it would take nearly two years to gather enough data to be in a position to apply for a disqualification, and a further four before legal proceedings would have finished.[172] Following these two reports, steps were taken to address the concerns identified. The NAO's second report,[173] published during the 1998-1999 session, expressed that the changes implemented had significantly increased the effectiveness of the system,[174] which had led to an overall sharp increase in the number of disqualifications year over year. The NAO identified the obvious relationship between the administrative efficiency of the IS in dealing with investigations and the effectiveness of the regime itself.[175] Despite the positive changes in reporting the NAO commented that the amount of time taken, on average, to actually issue disqualification

---

[167] ibid 16-25.
[168] ibid.
[169] NAO Report (n 124).
[170] ibid 2.21.
[171] ibid, para 2.21.
[172] ibid, 4.11.
[173] NAO Follow-Up Report (n 15).
[174] ibid 6.
[175] A point also made by Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 1.15.

proceedings against an individual had remained the same, and this was still therefore an area that ought to be improved upon.[176] This section will now continue to explore these early criticisms in order to assess whether problems of old have truly been resolved.

Reporting Unfit Conduct

2.22 Primarily, the SS is made aware of misconduct following reports submitted by officeholders. As such, it is clearly crucial to the effectiveness of the regime that they are received promptly by the IS so that investigations can commence, but also that they are of sufficient quality. Prior to the implementation of the SBEEA 2015, when investigating an insolvent company, IPs were required to submit a report in circumstances where it appeared to them that the conduct of a director[177] made them unfit to be concerned in the management of a company.[178] Initially they would submit an interim 'D2 return' within 6 months of the date of insolvency, followed by a more detailed (and final) report on unfit conduct known as the 'D1 return'.[179] The IP was expected to submit the D1 return within approximately nine months of the D2.[180] This system however was subject to numerous criticisms. These may be summarised as follows:

---

[176] NAO Follow-Up Report, para 2.32.

[177] Defined as a person appointed as such either at the time of the insolvency, or within the past three years: CDDA 1986, s 7(1).

[178] CDDA 1986, s 7(3).

[179] The D1/D2 returns were statutory forms set out in The Insolvent Companies (Reports on Conduct of Directors) (Amendment) Rules 2001. For more detail generally on returns and the time limits see: Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) paras 3.12-3.16.

[180] ibid para 3.13.

(a) the statutory, paper-based, D1 and D2 forms were outdated, being last amended in 2001, and were not fit for purpose given the technological and digital shift in recent years;[181]

(b) as a supplementary point, the forms were out of alignment with the Government Digital Strategy, which would require online submission of reports;[182]

(c) the timeliness of IPs in supplying the information was variable, and only 68 per cent were submitted within six months. This was largely due to the fact that IPs would often 'delay their reports whilst they…[satisfied]…themselves that they…[had]…sufficient evidence of misconduct';[183]

(d) the quality of the information supplied by IPs was variable. Although most were good, some lacked sufficient detail or relevant records so that cases could be investigated properly.[184]

2.23 Given the *then* two-year limitation period for the SS to pursue individuals for disqualification, the above factors had a considerable impact upon the outcome of any individual case.[185] The danger of course was that proceedings could not be commenced against persons worthy of disqualification because of administrative inefficiencies. If the system of reporting is inefficient this has a trickle-down effect on the effectiveness of the entire regime. This was recognised by the state and, following the IS's *Red Tape Challenge* consultation,[186] set to change. Section 107 of the SBEEA 2015 now provides for an entirely new system of reporting on the conduct of directors by insolvency officeholders.

---

[181] DBIS, 'Impact Assessment - Changes to reporting on the conduct of directors by insolvency office-holders. Red Tape Challenge Measure' (2014) available at <http://bit.ly/2vM8A9F> accessed 14 April 2017, para 18 (Reporting Impact Assessment).
[182] ibid, para 19.
[183] ibid, para 20.
[184] ibid.
[185] ibid, para 21.
[186] IS, 'Red Tape Challenge - changes to insolvency law to reduce unnecessary regulation and simplify procedures: Consultation' (2013) available at <http://bit.ly/2x9eBRW> accessed 14 April 2017.

2.24 Section 107 SBEEA 2015 implemented a new section 7A CDDA 1986.[187] It requires a report to be made to the SS as to the conduct of *all* directors of an insolvent company. The report must 'describe any conduct of the person which may assist the SS in deciding whether to exercise the power [to seek an undertaking or apply for a disqualification order]'[188] and be supplied within three months of the insolvency date.[189] There is a further obligation to supply any new information to the SS, when it becomes available, as 'soon as is reasonably practicable'.[190] The old D1 and D2 forms have thus been replaced with a single electronic form, submitted by IPs utilising the IS's Director Conduct Reporting Service ('DCRS') as of 6 April 2016.[191] It is understood that the new electronic return is shorter, with much of the information being pre-populated based on information already submitted, and with an ability to select from specified list of outline behaviours which may indicate misconduct, though with an additional 'free text' box to specify other matters.[192] Mark Danks, part of the insolvency targeting team at the IS, has commented that the DCRS was at the time of launch 'very much a basic application'[193] that simply met the terms of the legislation. As time moves forward, new features and a more refined reporting experience are expected to be introduced. In

[187] Section 7A is also supplemented by secondary legislation: The Insolvent Companies (Reports on Conduct of Directors) (England and Wales) Rules 2016. Moreover, full guidance notes for IPs are provided: IS, 'Company Directors Disqualification Act 1986: Interim Guidance Notes for the use of the Director Conduct Reporting Service' (2016) available at <http://bit.ly/2wkPavS> accessed 10 August 2017.
[188] CDDA 1986, s 7A(3).
[189] CDDA 1986, s 7A(4).
[190] CDDA 1986, s 7A(5).
[191] See the IS intelligence and enforcement leads comment: Gareth Allen, 'Director Conduct Assessment Service' Recovery (R3, Spring 2016) 38.
[192] IS, 'Red Tape Challenge - changes to insolvency law to reduce unnecessary regulation and simplify procedures: Consultation' (n 186) para 199.
[193] Mark Danks, 'The engine that drives director conduct reporting' Recovery (R3, Autumn 2016) 13.

particular, the author notes that the three-month time period is a considerable change, thereby allowing the IS to proceed to the investigation stages far more rapidly than was formerly possible. Moreover, given the 'new information' provisions, IPs should be less inclined to 'wait and see' before submitting their reports. It would seem that the extension of the limitation period for obtaining disqualification to three years, fits hand in glove alongside the new reporting requirements. Although it will not avert the substantive difficulties this surely an important step forward.

Resourcing Concerns at the IS

2.25 Since the introduction of undertakings, the Investigations Unit at the IS have seen an increase in workload. Yet, in 2010-2011 the Service experienced an 11 per cent budget cut, and 18 per cent of their workforce left under a voluntary exit scheme.[194] The cuts in the workforce were ascribed to an overall *reduction* in case load since December 2009,[195] though concerns were expressed at the time that it might 'put undue pressure on [the IS's] ability to deliver'.[196] Indeed, a report by the DBIS Select Committee in 2013 suggests that resource constraints, both in terms of staff and funding, have had a negative impact on the enforcement regime.[197] The report noted evidence from the trade union Prospect, which indicated that resourcing issues had led to the IS being 'unable to meet its internal target for the progression of disqualification investigations',[198] and that some cases had simply been abandoned.[199] Moreover, in the 2012 IS *Stakeholder Confidence Survey* one-third of IPs cited lack of resourcing as being a weakness of the

[194] DBIS Committee, *The Insolvency Service: Sixth Report of Session 2012-13* (HC 2012-13, 675) para 10.
[195] ibid, para 17.
[196] ibid, para 21.
[197] ibid, para 28.
[198] ibid, para 54.
[199] ibid.

IS.[200] It was also submitted in evidence to the BIS Select Committee by R3 that, whilst the number of D1 returns submitted by IPs had risen, the number of disqualifications had dropped in the same period.[201] A small 21 per cent of D1 reports were being taken forward to disqualification at that time.[202] Despite this, however, the IS stated that it '[was] confident that it [had] emerged [from the cuts] in good shape after a challenging period'.[203] The central point here is that an improperly resourced IS fundamentally weakens and destabilises the entire enforcement regime. This is of particular concern given the introduction of compensation orders and undertakings, which will only increase this burden.[204]

Timeliness

2.26 The most important consideration, resulting from a combination of the above two matters, is the impending statutory limitation period. Resourcing and reporting concerns ultimately leave the IS with a reduced amount of time to deal with the investigation and prosecution of cases. In some instances, this may result in a failure to secure a disqualification, or a complete abandonment of otherwise fruitful cases. This inevitably has an impact upon eventual enforcement outcomes, and thus the effectiveness of the regime. By the time D1 returns had been assessed the IS had, under the old two-year limitation period, approximately 12 months to investigate cases for disqualification.[205] An Impact Assessment produced by DBIS suggests that in a

---

[200] IS, *Stakeholder Confidence Survey 2012* (n 131) 50.
[201] DBIS Committee (n 194) para 58.
[202] ibid.
[203] ibid, para 109.
[204] 2.34
[205] DBIS, 'Impact Assessment – Extending the time limit for director disqualification proceedings under the CDDA' (2014) available at <http://bit.ly/2elSFZn> accessed 14 April 2017, 6.

'minority' of cases this was insufficient.[206] In those instances the IS had two options: either to issue protectively, or to allow the limitation period to lapse and seek permission to issue out of time. Both circumstances have obvious costs implications for the IS[207] and create uncertainty for the director involved. Thus, the longer limitation period should provide more flexibility for the IS in managing its caseload and permit, without prejudicing the interests of directors by any measurable degree, more complex cases to be seen to successful resolution. The author retains some scepticism as to the motive behind increasing the limitation period, however. Although heralded as a means of allowing the IS to deal with more complex (and thus potentially more serious) cases, it is suggested here the reality may be that it simply gives the IS the breathing room it needs in order to stabilise itself – to 'catch up' – following a harrowing period of cuts and redundancies.

Summary

2.27 Undoubtedly, disqualification has suffered with administrative difficulties since its inception. As explored above, this has a clear bearing on the effectiveness of the regime. Such matters are clearly important cogs in the overall machinery – though, it is submitted, they are by no stretch of *sole* importance. Indeed, as shown, considerable efforts have gone in to remedying administrative inefficiencies. Though, it is argued, one primary issue of concern as to the future of disqualification is that, due to the obsession with administration, sight has been lost in ensuring that the more substantive issues are dealt with. As the next chapter will explore, this is compounded by the fact

Presumably, given the extension of the limitation period by one year this will now mean the IS has approximately 24 months of investigation time.
[206] ibid 6.
[207] The IS approximates that it spends between £35,340 and £115,340 on such matters on an annual basis, ibid 3.

that the IS's primary means of assessing effectiveness is *not* in the adherence to the underlying objectives of disqualification (as this author suggests ought to be the proper measure), but in meeting bureaucratic and arbitrary targets.[208] Put simply, the DBEIS adopts the view that the more disqualifications, the better – but it looks not much further than that. Thus, the IS is incentivised to oil the wheels of disqualification to increase its efficiency (and will no doubt continue to do so), but no similar urge is felt in terms of remedying other, underlying, concerns so long as targets are met. The position of the state in this author's mind is therefore to do little more than 'keep up appearances' by patch working an already broken system. Some of these underlying concerns are dealt with in the next sections.

THE MEANING OF 'UNFITNESS'

2.28 There have been numerous stumbling blocks in the interpretation of section 6 CDDA 1986 generally which, by way of a reminder, provides a power to disqualify a person whose conduct 'makes him unfit to be concerned in the management of a company'. It will be remembered that section 6 is particularly important in this context, as the vast majority of disqualifications are made under this section. It is submitted, therefore, that difficulties associated with section 6 are likely to have a profound effect on the effectiveness of the regime as a whole. Perhaps the greatest challenge has been the meaning of the word 'unfitness' itself.

2.29 If it cannot be said with any certainty what conduct might actually lead to disqualification for unfitness, not only does this have significant implications for

[208] 3.24

objective of raising standards, as discussed previously, but also the deterrence objective. In other words, directors cannot be deterred from conduct that they do not know is, in fact, *mis*conduct.[209] In turn, this has wider ramifications for the primary objective of protecting the public from that misconduct. It is therefore submitted that clarity in respect of the meaning of unfitness, both in the orders and undertakings landscapes, is an essential ingredient to a successful regime. No definition of 'unfitness' is to be found within the CDDA 1986, and so some general rules of construction of the term have emerged in the case law. In *Re Sevenoaks Stationers (Retail) Ltd*[210] Dillon LJ set out that no judicial gloss ought to be placed on the meaning of the word, and that it was to be given its ordinary meaning.[211] Hicks argues that the problem with this approach is that 'judges [must] intuitively know what constitutes unfit conduct'.[212] Simply put, judges and the SS are expected to know unfitness when they see it. Moreover, in *Re NCG Trading Ltd*[213] it was made clear that conduct rendering a director unfit in one case is not necessarily conclusive of making such a finding in another. In essence, determining what type of conduct might render a director unfit in any given circumstance is little more than a 'value judgement' in the application of common sense principles. Judicial inquiry as to all of the circumstances, as opposed to a simplistic 'tick box' approach to a finding of misconduct, is no doubt desirable. However, as Hicks argues, this causes a further difficulty of 'creating and applying a consistent standard of unfitness both in the initial screening processes and in the courts'.[214] Hicks also doubts whether it is realistic

---

[209] A point also identified both by Hicks and Williams: Hicks, 'Director disqualification: can it deliver?' (n 138); Williams, 'Disqualifying Directors: A Remedy Worse than the Disease?' (n 139).
[210] [1990] BCC 765 (CA).
[211] ibid 773.
[212] Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 40.
[213] [2004] EWHC 3203 (Ch).
[214] Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 40.

to expect a court, in all cases, to be able to intuitively and accurately make such a finding. He suggests that judges may be faced with having to consider the issues perhaps without very much experience of the realities of commercial decision-making during their own careers.[215] This is potentially just as problematic, if not more so due to the presence of bias, in the case of undertakings, as directors will be clueless as to the internal processes and policies used by the SS in determining unfitness. Hicks goes on to criticise the position as being a 'legalistic approach to a highly practical matter'.[216] It is accepted that unfitness is very much a subjective term that, to use the terminology of one IS employee, 'means different things to different people'.[217] This inevitably creates room for error. However, the fault here does not lay solely at the feet of the judiciary.

2.30 Although the term is not defined in the CDDA 1986, a non-exhaustive list of factors to be taken into account by the court or SS in determining unfitness exists in the form of Schedule 1. Schedule 1 therefore presents itself as being the only form of Parliamentary indication as to the intended approach of the courts and SS in assessing unfitness. Effectively, it is a non-exhaustive list of factors that must be taken into account when either the court or SS is considering disqualifying a person. As part of the raft of changes introduced by the SBEEA 2015, Schedule 1 was repealed and replaced for reasons to be explored. Before this, the Schedule had not seen any significant modifications for over 30 years. The current implementation of Schedule 1

---

[215] ibid.

[216] ibid 45.

[217] David Henry 'Disqualification of Directors: A View from the Inside' in Harry Rajak (ed) *Insolvency Law: Theory and Practice* (1993 Sweet & Maxwell) as quoted in Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 40.

came in to force as of 1 October 2015.[218] At the time of writing, therefore, the practical implications of it have not yet been felt. The chapter will therefore go on to consider the position pre-SBEEA 2015 ('old' Schedule 1) as against the current implementation ('new' Schedule 1) in order to assess its potential utility.

2.31 The first thing of note in relation to 'old' Schedule 1 is that it is extremely statute heavy. Whilst it includes matters such as misfeasance and breach of duty, considerable focus is placed on administrative matters and, as Williams notes, financial harm to creditors.[219] This led to considerable criticism of the fitness for purpose of the Schedule. Hicks argued, discussing 'old' Schedule 1, that it was 'narrow and technical'[220] and '[did] not lay down positive standards of best practice towards creditors'.[221] The technical and legalistic approach to the question of unfitness taken by Parliament in Schedule 1 of the Act appears at least in part to have been driven the judiciary down the same path, as alluded to previously. A cursory reading uncovers a serious, yet elementary, point as to whether the average entrepreneur would have been able to understand and adopt the spirit of the Schedule in any meaningful way. It is suggested that they would have not. This may have been an unanticipated by-product of design, given it was likely drafted with its target audience, that being the courts and SS, in mind. This had significant ramifications for directors who, in turn, faced an ever-increasing regulatory burden. The real problem with 'old' Schedule 1 and the approach of the courts when considering the aims of disqualification, it is argued, is that it prevented

---

[218] By regulations: The Small Business, Enterprise and Employment Act 2015 (Commencement No. 2 and Transitional Provisions) Regulations 2015, SI 2015/1689.
[219] Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 4.27.
[220] Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 77.
[221] Hicks, 'Director disqualification: can it deliver? (n 138) 441.

directors from, as conclusively and comprehensively as possible, being able to determine whether any particular action might lead to their disqualification later down the line. There is no magic formula for unfitness. Whilst this creates flexibility for the judiciary and SS, it has the consequence of significant uncertainty for directors. Therefore, to the return to the original problem, due to the approach of the courts and SS, there is no straightforward means of ascertaining whether any particular conduct may render a person unfit.

2.32 Two things therefore follow from that conclusion. Firstly, that it is unsurprising that so many directors are disqualified for what appear at face value to be rather trivial matters,[222] given that they have limited means of knowing what is right, and what is wrong. Granted, the number of individuals that would in any case seek out that information proactively is likely to be small. However, even those that do so would be required to trace through and decipher numerous case law authorities and the CDDA 1986 itself; possibly none the wiser at the end of the process. The mere fact that there is a lack of comprehensible material outlining the circumstances in which a director may be disqualified is considered by this author to be a significant failure. Turning to the second point, this failure is made more acute by the fact that directors cannot be deterred, in accordance with the aims of the regime, from misconduct that they simply do not know, or have no means of knowing, impinges upon their fitness to act. It is therefore ultimately concluded that this approach to determining unfitness at best fails to maximise the potential effectiveness of disqualification. It creates an uneven playing

[222] The word 'trivial' is used here rather glibly. It is meant only insofar as to say that some directors appear to be disqualified for very minor transgression indeed: 3.20.

field in a situation where the commercial decision-making of directors is placed under microscopic scrutiny. Fortunately, this was a point recognised in the *Transparency and Trust* consultation,[223] which led to the implementation of 'new' Schedule 1. It was accepted that often directors will have considerable difficulties in knowing where they stand and that this was crucial to the effectiveness of the regime.[224] Indeed, the author has no hesitation in suggesting that this particular deficiency of 'old' Schedule 1 has hindered the success of the regime at least in part for some three decades. This is not, however the only criticism to be levelled at the Schedule. With it setting out a non-exhaustive list of factors, this has inevitably led to significant judicial energy being expended on determining whether specific types of misconduct, upon which the Schedule is silent, might evidence unfitness in any given case. Again, this was recognised in the Consultation.[225] It is doubtful, however, that the Schedule should ever have been, or be, so specific so as to list individual matters that demand a finding of unfitness. The reason for this is aptly summed up in the Government Response:

> [A]ddressing this issue simply by adding to the list…[is]…not appropriate – this might feed any unhelpful belief that if a matter is not explicitly listed, it will not be taken into account by the court or the SS. It seems that it is the list itself that is the problem.[226]

Moreover, if the Schedule is to be non-exhaustive (which it is argued it ought to be) it would be of limited value to list individual forms of misconduct in any case. The court or SS could simply go behind it in appropriate circumstances, albeit at the potential cost

[223] DBIS, 'Transparency and Trust: Enhancing the Transparency of UK Company Ownership and Increasing Trust in UK Business – Government Response' (April 2014) <http://bit.ly/1no7pXg> accessed 01 August 2016, para 271 (T&T Government Response).
[224] ibid, para 206.
[225] ibid, para 205. By way of example, Williams notes that 'trading to the detriment of the Crown' – one of the most prominent forms of reported misconduct in undertakings cases – is simply not covered by the Schedule. This has in turn led to a whole raft of case law on the point: Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 4.36.
[226] T&T Government Response, ibid para 221.

of further litigation. The difficulty for the draftsperson is therefore to ensure that the Schedule is accessible to the wider public at large so that they know where they stand, whilst avoiding the creation of an ever-growing list of specific instances of misconduct akin to an 'instruction manual', that can in any event be abandoned. Ultimately, the Government concluded that the 'old' Schedule 1 was outdated and lacked transparency.[227] It was therefore pledged that the old Schedule 1 would be replaced with a *generic* set of (non-exhaustive) factors, rather than focusing on specific forms of misconduct.

2.33 'New' Schedule 1 is therefore far less verbose than its predecessor. Existing references to statutory provisions have been vanquished and instead catch-all phraseology is utilised, such as 'any material contravention…of any applicable legislative…requirement', in its place. References to misfeasance or breach of duty are maintained. However, a new provision is introduced requiring the court or SS to consider '[t]he nature and extent of loss or harm caused, or any potential loss or harm' as a result. Importantly, the *frequency* of the misconduct is now a requirement for consideration. Given the relatively recent introduction of the Schedule, it is difficult at this point in time to accurately reflect on how its implementation may affect the disqualification landscape. At the very least, it can be said that there has been some recognition on the part of the state that defining unfitness is problematic, and that they have sought to address it. From the point of view of accessibility, it is certainly true that it is drafted in a way that is more understandable to the layperson. This should ease some of the criticisms levelled by those such as Hicks. The 'new' Schedule, in fact, is

[227] ibid, para 220.

a relatively untechnical document. To use the terminology of Williams, who discussed 'old' Schedule 1, the State has moved away from a largely 'rules-based' approach to a more 'standards-based' one.[228] The adoption of a more generic set of guiding principles is to be applauded, and it ought to have some wider impact upon the cost and ease of administering the disqualification regime.[229] However, the author is still sceptical as to whether 'new' Schedule 1 will assist with achieving the desired deterrent effect given that directors must still, of course, go out of their way to discover the information. Individuals cannot be expected to absorb legislative changes by osmosis; no matter how comprehensible they might be. As has been shown, CH do not take steps to notify directors of legislative changes, including Schedule 1, in an all-encompassing way. Awareness is therefore still likely to be low. It will be interesting to see how the courts approach 'new' Schedule 1 in practice, though it is unlikely to herald much change for directors. Undoubtedly, though, the tempering of existing confusion that had been known to arise out of the application of the predecessor Schedule is to be welcomed.

COMPENSATION ORDERS AND UNDERTAKINGS

2.34 This section looks in detail at the newly enacted regime of compensation orders and undertakings. This is surely the most radical reform to disqualification since its original inception. In effect, it permits recovery for creditors by rendering a delinquent director personally liable for losses incurred as a result of her misconduct, in a similar way to the private enforcement mechanisms discussed subsequently. However, it blends

---

[228] See generally, Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) paras 4.28-4.36.

[229] Administrative concerns are dealt with below: 2.21.

this function with public regulation.[230] It empowers the SS to apply to the court to seek a compensation order against a disqualified director for the benefit of a defined creditor or creditors of an insolvent company, or as a general contribution to the company's assets, within two years of the disqualification start date.[231] A director may also offer a compensation undertaking to the SS should they wish to avoid court proceedings.[232] As indicated in the first chapter of this thesis, it is presently impossible to judge the effectiveness of these new provisions on the basis that there is simply no data to consider.[233] This section will therefore go on to examine some of the issues that may help or hinder their *potential* effectiveness, which will then be supplemented by empirical findings in the next chapter. On the face of it, the changes are innovative in an area that has gone virtually untouched by way of reform for some two decades. Moreover, they may transpire to be welcome, as they provide yet a further avenue of recovery for creditors thus enhancing the direct protection objective of disqualification.

The Legislation

2.35 *The power* The provisions themselves are contained within Part 9 of the SBEEA 2015, specifically section 110. That section amended the CDDA 1986 to add sections 15A-15C. The provisions were brought in to force on 1 October 2015 by Regulations.[234] Section 15A(1) provides that the court may make a compensation order against a person on the application of the SS. Under section 15A(2) the SS may instead accept a

---

[230] Williams suggests that 'the new powers have the potential to significantly increase the importance of 'public' regulatory proceedings in corporate insolvency', See: Williams, 'Civil Recovery from Delinquent Directors' (n 125) 312.
[231] CDDA 1986, s 15A(1); for limitation period see s 15A(5).
[232] CDDA 1986, s 15A(2).
[233] 1.12
[234] The Small Business, Enterprise and Employment Act 2015 (Commencement No. 2 and Transitional Provisions) Regulations 2015, SI 2015/1689, reg 2(f).

compensation undertaking from an individual. Both subsections are subject to the proviso that the two conditions under section 15A(3) are met. That subsection reads:

> **15A(3) The conditions are that –**
>
> (a) the person is subject to a disqualification order or disqualification undertaking under this Act, and;
>
> (b) conduct for which the person is subject to the order or undertaking has caused loss to one or more creditors of an insolvent company of which the person has at any time been a director.

One additional matter worthy of attention is set out in section 15A(5), which defines a limitation period of two years from the date the disqualification order was made, or the undertaking was accepted.

2.36 The requirements to seek compensation are thus summarised by the author as being:

> (a) the misconduct must have been committed by a director on or after 1 October 2015;
>
> (b) the company must be insolvent;
>
> (c) the director in question must have been disqualified for misconduct in relation to that company;
>
> (d) the loss suffered by the creditor(s) must be identifiable and able to be attributed to the director's misconduct leading to the disqualification;
>
> (e) no more than two years from the start date of the disqualification must have elapsed.

The requirement that some loss is caused, given the compensatory agenda of the legislation, is no great surprise. A director cannot therefore be pursued on principle for what might be described as nominal damages. Moreover, Section 15A(3)(b) guarantees that all compensation cases will involve insolvent companies. Given that disqualifications pursuant to section 6 CDDA 1986 for 'unfitness' also require insolvency, it seems likely that it is anticipated that the bulk of compensation claims will arise out of section 6 disqualifications. The business of insolvency naturally involves an expectation that some loss will have been incurred somewhere along the line. For that reason, the inability of the SS to establish the 'loss' criterion is likely to be reserved for the rarest of cases. However, there is also a causation requirement between the conduct of the director in question and the loss. The wording of the provision suggests that any conduct not forming part of the original basis for the disqualification will fall outside of the scope of the compensation provisions. In any event, the burden of proof clearly rests on the SS to prove the causal link between the misconduct and the loss. The causation requirement therefore provides something of a safety net for disqualified directors, ensuring that their exposure is not 'unlimited'. It ensures that compensation will only be obtainable in those cases where the loss can be shown to be a direct result of their misconduct, and this, it is suggested, is demonstrative of an underlying intention to protect creditors in accordance with the objectives of disqualification; rather than to punish errant directors. The final stipulation of section 15A(3)(b) – that a person can be held liable to compensate if he has been a director *at any time* – is also worth identifying. This mirrors the existing provisions for disqualification orders and undertakings, to ensure that retired directors, or even those forcibly removed from office, cannot escape liability. Of course, it should be remembered that only the SS has *locus standi* to bring an application for compensation order, or seek an undertaking. As such, creditors are unable to avail themselves of the power directly. Thus, to a significant degree, their prospects of recompense and therefore the success of the regime is based upon the policy of the SS in deciding which cases to pursue, and the success rate in doing so.

2.37 *Allocation of compensation* Section 15B(1) sets out the three ways in which compensation can be allocated under a court order. Section 15B(2) places undertakings on the same footing as orders in this regard. An order can be made to require a disqualified director to compensate: one or more creditors; a class or classes of creditor; or by way of a contribution to the general assets of a company. There is no stipulation that the three types of allocation are mutually exclusive and so it is possible that a director may be required to make multiple compensatory payments depending on the circumstances, perhaps one amount to an individual creditor and another to the insolvent company's assets.

2.38 *Determining the amount* In determining the quantum of the compensation section 15A(3) provides a non-exhaustive list of three factors that either the court (in the case of an order) or the SS (in the case of an undertaking) should have particular regard to. They are as follows:

(a) the amount of the loss caused;

(b) the nature of the conduct mentioned in section 15A(3)(b);

(c) whether the person has made any other financial contribution in recompense for the conduct (whether under a statutory provision or otherwise)

It is logical to assume that the starting point for determining the amount of compensation to be awarded should be the debtor company's liability to the relevant creditor at the time of the order or undertaking. Specific focus should be placed upon the portion of the liability proven to have been caused by the director's misconduct. It was stated in an Impact Assessment published by the IS that the amount of compensation awarded should never exceed the loss caused,[235] which again reinforces the notion that the regime is not designed to be punitive, merely restorative. Whilst acknowledging the difficulty of calculating the prospective amount of compensation directors might be expected to pay, the IS calculated an average of approximately £132,000, based on a sample of 26 cases considered by debt recovery agents.[236] This point will be revisited in some depth in the next chapter when considering the solvency of disqualified directors.[237] In short, the author is sceptical, when considering the largely owner-manager demographic, as to the number that would be sufficiently personally solvent to be able to satisfy such claims in any case, thereby bringing the potential utility of the section in to question.[238]

Objectives and Rationale

2.39 As part of the coalition government's agenda of identifying measures to increase the level of trust and stakeholder confidence in UK company law, DBIS conducted the *Transparency and Trust* consultation.[239] The consultation also included significant proposals in relation to disqualification. Evidently a perception exists within society that delinquent directors rarely suffer financially and, in the main, 'get off lightly' given the circumstances of their misconduct.[240] Although disqualification currently helps to

---

[235] DBIS, 'Impact Assessment – Giving the court and Secretary of State (SoS) a power to make a compensatory award against a director' (2014) available at <http://bit.ly/2esCrRH> accessed 14 April 2017, para 23.
[236] ibid para 56.
[237] 3.57.
[238] A point also made by Williams, 'Civil Recovery from Delinquent Directors' (n 125) 324-332.
[239] T&T Discussion Paper (n 14).
[240] To give but a recent example that attracted a considerable amount of media attention, note the administration of retailer British Home Stores; leading to a sizable pensions deficit in the company as well as the redundancy of a large number of employees. There were a number of calls for Sir Philip Green to be taken to task for his involvement in the company – whether disqualification was an option is unknown. Though, at the time of writing, it is noted that Green's successor to the company, Dominic Chappell, is being pursued criminally by the Pensions Regulator: See 'BHS

minimise phoenix syndrome by preventing a director from acting in future, a frequent criticism of it in the past has been that it does little for the creditors actually affected.[241] This may now be set to change. Creditors, it is suggested, are likely to be advocates of robust recovery mechanisms, rather than regulatory procedures. Thus, it is unsurprising that the government's response to this criticism comes in the form of the compensation provisions. Throughout the legislative process, the driving factors behind the reforms were stated as being:[242]

(a) to improve stakeholder confidence in the enforcement regime, and;

(b) effect a change of behaviour in directors;

(c) whilst providing better recourse to suffering creditors.

As a natural extension of it, it is unsurprising that these objectives can readily be associated with the underlying objectives of the general disqualification regime. The idea is that through increased accountability for directors, the trust and confidence of stakeholders will increase in turn. Indeed, from a corporate governance perspective, it has the merits of promoting good stewardship, as well as being yet a further deterrent to director misconduct. As has been set out previously, a by-product of the specific deterrence is that it may generally raises standards of management which, from a corporate governance perspective, is no doubt welcome. Appealing to the needs of creditors and having a general appearance of being 'tough' on directors is surely key to increasing this confidence. It is also thought that by increasing the accountability of

---

owner Dominic Chappell prosecuted by Pensions Regulator', *The Telegraph* (22 August 2017) available at <http://bit.ly/2glLqRQ> accessed 30 August 2017; 'Sir Philip Green's reputation 'still stained' despite BHS pension deal', *BBC News* (1 March 2017) available at <http://bbc.in/2lborhw> accessed 30 August 2017.

241 Hicks, 'Director disqualification: can it deliver?' (n 138); Williams, 'Disqualifying Directors: A Remedy Worse than the Disease?' (n 139).

242 DBIS, 'Impact Assessment – Giving the court and Secretary of State (SoS) a power to make a compensatory award against a director' (n 235) 1.

directors in this way standards will be raised. If it is to be effective, however, there must be a 'seen' effect in the actual compensation of creditors. Primarily, it should therefore allow better recourse for those affected by misconduct, in a way that the law has not previously provided for. As Williams notes, whether the net level of recovery for creditors will increase in practice is unclear.[243] In furtherance of that point, this section will therefore now continue by identifying some of the potential barriers to the success of the compensation mechanism.[244]

Pressures on the IS

2.40 The two-year clock for the SS to obtain compensation begins to run when the original disqualification order is made, or the undertaking is accepted. With what is arguably backwards thinking, one of the reasons for the recent increase from two years to three of the limitation period for disqualification *proper*, it seems, stems from the fact that the IS has in the past been under-resourced to the point of being unable to conclude cases within the limitation period. Thus, instead of leading to a proper resourcing of the Investigations Unit, it merely drove an extension of the limitation period. In order to secure a compensation order or undertaking it is clear that additional investigations, beyond those currently conducted, will be required. Naturally this has further implications for the IS with respect to the time and cost involved. It has been estimated that investigation costs for each case considered for compensation may rise by 20-50 per cent.[245] Despite failings in the past, there is some hope that they will not

---

[243] Williams, 'Civil Recovery from Delinquent Directors' (n 125) 322.
[244] To be further expanded upon following empirical analysis in the next chapter: ch 3.
[245] DBIS, 'Impact Assessment – Giving the court and Secretary of State (SoS) a power to make a compensatory award against a director' (n 235) para 39.

translate in to the compensation regime. One reason for this is because much of the evidence gathered in order to a secure a disqualification in the first place will no doubt also be instrumental in obtaining a compensation order or undertaking. Much of the additional work required, it is suggested, will probably involve satisfying the causal link between the loss and the misconduct. Taken in conjunction with the extension of the limitation period, and simplified reporting requirements, it is hoped by the author that this will reduce the need for some of those criticisms previously expressed. In most cases, it has been suggested that compensation orders or undertakings would in fact be sought contemporaneously with the disqualification itself.[246] In any event, the IS has pledged to ensure that directors are fully informed, and have sufficient notice, should the intention be to pursue them for compensation.[247] At worst, however, a director may be embroiled in proceedings for up to five years.[248] Only time will tell as to whether the IS will be able to deal with the additional pressures placed upon it under the new regime. Further, questions should be raised as to whether additional resources will be secured to ease the burden currently suffered by the Investigations Unit, though recent accounts do not show any significant additional funding from DBEIS at present.[249] If resourcing is still a core difficulty within the IS, then it must follow that increasing the current workload to include compensation claims has the potential to diminish the effectiveness of the disqualification regime as a whole, if cases cannot be investigated and proceedings instigated in a timely manner.

---

[246] As stated by Vicky Bagnall, director of enforcement and investigation at the IS: Vicky Bagnall, 'The compensation regime' Recovery (R3, Winter 2016) 37.

[247] ibid.

[248] Unless, of course, the IS makes an application to the court to extend time as is the current practice in a small number of cases.

[249] IS, *Annual Report and Accounts 2015-16* (2016) <http://bit.ly/2tXPfF9> accessed 1 July 2017, 71

Competing Claims

2.41 Walton has raised concerns with regards to how the existing private recovery mechanisms, will interact with the new compensation legislation.[250] He suggests that there is a 'real risk that any compensation orders or undertakings being sought by the Secretary of State…may interfere with or prevent actions currently being taken by office holders'.[251] There are in effect two 'interference' arguments in the author's mind. Firstly, both parties (the office holder on the one hand, and the state on the other) may launch proceedings against the same individual, for the same or similar misconduct. If communication fails between the two parties, and thus the litigation is not properly orchestrated the consequences may be significant in terms of costs (to creditors, as well as the tax payer), as well as in hindering the efficiency of the regime. There are also clear difficulties in terms of double recovery, and the means of how this will be avoided is unclear. Vicky Bagnall, director of investigation and enforcement services at the IS, has stated that the process will require 'collaborative working'[252] and a 'continuous dialogue'[253] in order to avoid these issues. This may be all the more difficult to ensure given that, *inter alia,* wrongful and fraudulent trading claims can now be assigned to third parties as dealt with later in this thesis.[254] The IS will have to ensure sufficient communications with assignees so that proceedings are not launched needlessly; at cost to the taxpayer. It will therefore be interesting to see how these issues resolve themselves in practice, though the author retains some scepticism as to what rather

[250] Peter Walton, 'Insolvency litigation - a case of 'if it ain't broke, don't fix it?'' (2015) Insolv Int 9, 13.
[251] ibid 10.
[252] Bagnall (n 246).
[253] ibid.
[254] ch 5.

sounds like a haphazard approach at present. The second issue relating to interference is that officeholders may refrain from taking action against directors and instead 'sit and wait' for the SS to pursue a claim under the compensation provisions. The reasons for this are fairly plain, as Williams argues:

> [The risk of private enforcement litigation] would tempt many insolvency practitioners to pass issues of civil recovery to the SS, which after all, could well be the lowest-risk way of securing the highest compensation for creditors. Passing the costs of recovery to the state lowers the expenses of the liquidation through lower insolvency practitioner fees and creates no risk of litigation costs falling on creditors, enabling the office holder to achieve a better return for creditors in a shorter time scale.[255]

The result of which, he suggests, 'could have the effect of encouraging insolvency practitioners to shift the financial burden of civil recovery from the estate of insolvent corporations to the state'.[256] As to this point, however, Bagnall has rather conclusively stated that:

> [The IS] certainly don't want to bring proceedings where the IP is already contemplating recoveries for the same misconduct…[so] we expect that in many cases, the office-holder will continue, as now, to take recovery action.[257]

As an initial point, to state that 'in many cases' the officeholder will take action (i.e. the state *will not*) is surely to concede that the section will have limited application in a very small number of cases. More substantively, again, this seems something of a haphazard approach to the issue. Without a clear implemented policy, as to how the differing interests between the various stakeholders is to be managed, it is suggested that Walton's fears are highly likely to become a reality. The whole issue can be reduced to that of costs: the state will commence proceedings in the public interest, at its own cost, but it will only do so where private financing is unavailable as its resources are limited. The officeholder, on the other hand, who is tasked with ensuring the best return for

[255] Williams, 'Civil Recovery from Delinquent Directors' (n 125) 322.
[256] ibid.
[257] Bagnall (n 246).

unsecured creditors, is incentivised to decline to take action so that it may be funded by the state. The author therefore has in mind a rather childish stalemate type situation, where each party anxiously awaits to see whether the other will make the first move. Of course, the danger is that in the end *neither* makes a move in a timely fashion (considering the two-year limitation period), thereby hindering returns for creditors and the effectiveness of the regime, as compared with the previous system. It goes without saying, that this is no way to go about the very serious business that is disqualification. It is therefore unsurprising that Bagnall is intently willing on the need for a strengthened collaboration with IPs, given that this particularly fragile link in the chain may lead to the undoing of the compensation regime, before the benefits of it have even begun to take effect.

'Cherry Picking'

2.42 The Impact Assessment suggested that the SS may pursue directors for compensation particularly where vulnerable members of the public (perhaps consumers) are concerned, or where there are large numbers of unsecured creditors.[258] That aside, it also made clear that compensatory awards would only be sought against directors in the most serious of cases.[259] The level of seriousness of a case is thought to be gauged with reference to the period for which a director is disqualified, in line with the *Sevenoaks* brackets. It is assumed by the author therefore that the IS would only consider pursuing those cases where a disqualification is for a period in either the middle or upper *Sevenoaks* brackets (i.e. greater than five years), given that conduct in

[258] DBIS, 'Impact Assessment – Giving the court and Secretary of State (SoS) a power to make a compensatory award against a director' (n 235) para 42.
[259] ibid para 40.

the lower bracket is generally expressed as being 'minor'. The reason for this limitation is perhaps unclear. The legislation itself does not impose any criteria with regards to the severity of the misconduct. As previously discussed, it merely requires that a director has been disqualified under the CDDA 1986 and that there is some level of loss attributable to the misconduct. Whilst it provides that the severity of the conduct is a relevant factor in determining the quantum of the compensation to award, it does not impact upon a director's general exposure to liability. A question therefore has to be asked as to why the IS would choose to artificially limit the scope of the provisions by 'cherry picking' the cases to bring forward. There are several practical reasons why an action may not be pursued against any individual director, for instance, a lack of evidence, a director's inability to pay, or the balancing of investigative priorities (i.e. IS resource constraints).[260] However, these matters would not explain a steadfast policy of rejecting less serious cases. It is possible that the IS wishes to make an example of directors who commit serious misconduct, though it is submitted this would be counter to the objective of the legislation to protect; rather than to punish. Again, in a similar fashion to arguments put forward previously in this chapter, it is suggested that if the introduction of compensation is to shift the focus of the regime more forcefully into the territory of punishment, then the underlying disqualification framework ought to be revisited. One might also think that serious cases are more likely to involve the largest amounts of loss, and therefore be the most appropriate to consider for compensation. However, although the quantum of loss suffered is a consideration in compensation matters, it does not appear to be a factor considered when determining the length of the

[260] See Bagnall (n 246).

period of disqualification itself.[261] In short, it is not necessarily true that longer periods of disqualification are associated with any greater amount of loss. Thus, prosecuting these cases in particular may be no more or less advantageous, and there seems little rationale for discriminating between directors who have committed greater and lesser misconduct. Furthermore, it introduces uncertainty for creditors as to whether they will, in practice, be able to depend on the compensation provisions. Strangely, creditors have to rely on directors to be sufficiently improper so as to warrant proceedings being taken. This is in spite of the fact that increasing stakeholder confidence (presumably across the board) is a core aim of the regime. The author adopts the concerns of Sarah Paterson, who fears that the compensation regime may end up becoming a 'politically engaged remedy'.[262] Here, directors would be pursued for compensation only where potential losses to creditors or the seriousness of the misconduct is considered 'intolerable to public opinion'.[263] Such an approach if it materialises, of course, is difficult to square with the underlying objectives of either disqualification proper or the compensation mechanism.

Challenging Deterrence (Again)

2.43 The threat of compensation should, in theory, aid in the deterrence agenda of disqualification generally by ensuring that directors are more financially proximate to their own risk taking; thereby reducing the moral hazard problem, and deterring self-dealing or other misconduct. However, as Williams recognises, it will only do so where there is an 'increased likelihood of civil liability in disqualification as compared to the

[261] As shown empirically in the next chapter: 3.42.
[262] Sarah Paterson, 'Compensation orders: a quiet revolution' Recovery (R3, Summer 2017) 32, 34.
[263] ibid 34.

likelihood of sanction under existing rules'.[264] If effective, incidences of this behaviour should decrease, or at the very least not increase, and standards of company directors should therefore be improved overall. It should be reiterated that many of these same arguments have been made in favour of disqualification proper over the years; the fruits of which remain to be seen. However, instead of mere regulatory action by the State the new power permits personal assets to be touched. Therefore, it may be the key to reinvigorating the deterrence objective of disqualification. Despite this optimism, if the new provisions are to rectify issues of the past, there are several concerns that must be first addressed. Two distinct issues that may give rise to further or accentuated difficulties will therefore be examined below.

2.44 *Awareness* As set out previously, awareness amongst directors of disqualification proper is low. If the new compensation provisions are to be effective, the IS needs to revisit this issue. At the time of writing, the author is not aware of any such steps relating to compensation specifically. It will also be remembered that no action was taken by the State to notify directors of the new changes; save for information published on the IS and CH websites.

2.45 *'Cherry picking' revisited* The issue of the State 'cherry picking' cases to pursue for compensation, dealt with previously, also has some relevance in the specific context of deterrence. It is argued here that the artificial filtering of cases in such a way can only hinder the prospect of a successful deterrence agenda. It is of course to be expected that minor misconduct would not be placed on an equal footing with more serious misconduct. However, it is submitted that in outwardly maintaining a policy *not* to

[264] Williams, 'Civil Recovery from Delinquent Directors' (n 125) 335.

pursue instances of minor misconduct, this will not only fail to deter directors from it, but it may even go some way as to rationalise the behaviour; leading to directors feeling that they can 'get away with it'. As such, it is tentatively suggested it may go as far as to encourage certain types of misconduct. By the same token, due to the discriminatory element of the policy, those who are disqualified for serious misconduct and ordered to pay compensation, when those who commit misconduct at the lesser end of the scale are not considered, may be in fact justified in feeling that the proceedings are punitive and vindictive. Most importantly, in line with Loughrey's arguments, set out previously, this is again unlikely to effect a change in director behaviour.[265]

2.46 *Summary* In summary, although deterrence is merely one element, it is an important one. It is argued here that the introduction of compensation orders and undertakings presented an opportune time to rectify previous failings under the existing legislation. Based on the hypothesis that directors who face both financial and regulatory sanctions are more likely to conform to higher standards of management than those who merely face regulatory sanctions, it has the potential to occupy a far larger role in disqualification than it does at present. These arguments will be further expanded upon in the next chapter and, in particular, the penultimate chapter when dealing with general reforms.

THE COST OF CHALLENGING UNDERTAKINGS

2.47 The very purpose of introducing disqualification undertakings was to reduce the time and cost involved in obtaining court orders,[266] thereby reducing the burden on the

---

[265] 2.16.

[266] See Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 1.13.

taxpayer on the one hand, as well as anxiety for directors who would otherwise have to go through a protracted judicial process. To this end, it is clear that undertakings have done just that. One of the substantial criticisms[267] over the introduction of an undertakings regime however was that it would deny directors the right to 'have their day in court'. Of course, a director has always been free to *refuse* an undertaking (and thus have their day in court), but this may well be a false choice. As a trade-off for these efficiency savings, there is a not insignificant risk that some directors are coerced into giving an undertaking so as to limit any additional financial exposure – potentially even in cases where the evidence against them is weak. This is because the usual litigation rule as to the award of costs (i.e. that the claimant pays the defendant's costs on discontinuance)[268] is reversed in disqualification cases.[269] Directors therefore have to be especially mindful that if an undertaking is initially refused, they may face considerable financial consequences if they should later have a change of heart. This imbalance in relation to costs, when combined with the fact that the IS, in relative terms, has unlimited investigation resources at their disposal as against the individual director, who may be unable to even afford to instruct a solicitor, thus uncovers considerable potential for oppression to fester in the undertakings regime.[270] The survey conducted by Hicks in 1998 explored these issues somewhat.[271] It must be remembered that his survey pre-dates the introduction of undertakings, and therefore only concerns disqualification orders. However, this is useful as it details the type of costs that directors who seek to

---

[267] See for example the judgment of Sir Richard Scott in *Re Barings Plc* [1998] Ch. 356, 361; Williams, ibid para 1.21.
[268] CPR 38.6.
[269] PD on Directors Disqualification Proceedings, 25.1
[270] Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 1.21 (fn 59).
[271] Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 32.

challenge undertakings may ultimately be faced with. Hicks noted the average cost of defending was £18,000, though in some cases it ran in to the hundreds of thousands.[272] Moreover, adverse costs orders averaged at £7,800 though, again, some were much higher.[273] Hicks therefore estimates the total cost of defending proceedings to be in the region of £25,000-30,000.[274] In the survey, only 50 per cent defended disqualification cases and, amongst those that did not, the primary reason was that they could not afford to do so.[275] This led Hicks to identify that the most often cited reason (in 27 per cent of cases)[276] for directors finding the disqualification process to be unfair was the expense and complexity of the process.[277] Many thought that, in effect, they were denied access to justice; one particularly disgruntled director referred to the entire process as a 'gravy train' for lawyers and accountants.[278] Directors therefore simply 'rolled over' because, as Hicks summarises:

> They could not afford the time, energy and money to oppose the state machine with its apparently unlimited expertise and resources.[279]

2.48 *Owner-managers* Again, when one remembers that, by and large, most disqualifications are suffered by owner-managers of small concerns, the problem is magnified somewhat. Moreover, empirical research conducted by this author, set out in the next chapter, suggests that a small but noticeable proportion of disqualified directors suffer bankruptcy following the corporate insolvency.[280] Owner-managers, who are

---

[272] ibid.
[273] ibid.
[274] ibid.
[275] ibid 32-33.
[276] ibid 123.
[277] ibid 32-33.
[278] ibid 123.
[279] ibid 33.
[280] 3.57.

likely to be the only source of capital in their business, are known to plough personal funds into their ailing company in order to try and save it. A proportion of these directors will have given personal guarantees to banks or other lenders.[281] The reality is that many of the individuals in this demographic will have insufficient assets to be able to challenge even the threat of an undertaking in the first place. Thus, the idea of directors having a legitimate choice of being able to have their case heard before a court is, in many instances, almost certainly an illusory one.

2.49 *Compensation undertakings* It is further argued, for reasons that will now be obvious, that this potential for oppression is likely to become all the more noticeable once the compensation regime takes hold. Here, we are dealing with very large sums indeed. In terms of the cost of defending proceedings, as stated above, the IS has estimated an increase of 20-50 per cent in its own investigation costs.[282] If this is translated into the costs payable by those who seek to compensations undertakings, alongside the disqualification undertaking itself, in line with Hicks' figures, this may see legal costs easily exceed £50,000. Moreover, it will be remembered the average figure the IS suggested as being obtained for creditors was some £132,000.[283] Although this calculation is by no means an absolute science, it may be said that in a typical case a director will face having to pay sums bordering £200,000. If it is assumed that most directors will not be able to afford such sums, as this author does, then invariably they

[281] Judith Freedman and Michael Godwin, 'Incorporating the micro business: perceptions and misperceptions', in Alan Hughes and David J Storey (eds), *Finance and the Small Firm* (Routledge 1994) 232, 246 (where 54 per cent surveyed had given personal guarantees); Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 9 (where 75 per cent surveyed had given personal guarantees).
[282] DBIS, 'Impact Assessment – Giving the court and Secretary of State (SoS) a power to make a compensatory award against a director' (n 235) para 39.
[283] ibid 56.

will face two choices: bankruptcy, or challenging the undertaking(s). Relative to the principal amount of compensation, the issue of legal costs will invariably fall into insignificance. Therefore, there may be an argument to suggest that more directors *will* seek to challenge undertakings, given that in either circumstance they will ultimately be faced with bankruptcy proceedings anyway. Unlike what has been seen in the past, the scenario envisaged here could result in a significant proportion of directors wishing to take their chances with a court hearing as, simply put, they would have nothing to lose if bankruptcy is already a foregone conclusion. Given the fact that most disqualification and compensation undertakings will be sought contemporaneously,[284] this may leave these directors with little choice but to challenge *both* undertakings at increased cost. If this were to become a reality, the effectiveness of undertakings as being a time and cost saving initiative both for the courts and the general taxpayer, in this admittedly small subset of cases, would then be brought into question. It has been stated by the IS that they will only pursue those directors for compensation who, to put it bluntly, can afford to pay.[285] But, considering the demographic and solvency issues explored in the next chapter,[286] the author remains fundamentally sceptical, to put it rather simply, whether the IS will be able to find anyone that meets the criteria.

2.50 *Considering effectiveness* The issue of balancing the rights of individuals, and the need to protect the public from the abuse of limited liability (and deter others from doing so) permeates the entire fabric of public regulation in this area. The scope for oppression as regards costs brings the need for a fair balance more sharply in to focus.

[284] Bagnall (n 246).
[285] ibid.
[286] 3.57.

Should the proper balance not be maintained, then the interests of justice are compromised. Thus, the concerns expressed above in relation to oppression must be constantly guarded against by the IS if trust and confidence in the regime is to be maintained, and increased beyond current levels. The essential point is that bureaucratic concerns of the IS[287] should never trump the fair treatment of defendants in what is probably at the very least a quasi-criminal process.[288] The impact of the compensation regime, on the issue of oppression, may inevitably create some ripples given the huge financial stakes. As stated, this may lead to an increase in the number of challenges made thereby frustrating, at least in part, the underlying purpose of undertakings (including disqualification proper undertakings) and hinder the overall effectiveness of the regime in the process.

CONCLUSION

2.51 Being *ex post facto*, disqualification proper and the newly introduced compensation mechanisms are inevitably condemned to at least partial failure in protecting the public from abuses of limited liability. This chapter has gone some way in exploring a number of the prominent difficulties faced by the regime, and it has speculated on emerging difficulties – and opportunities – created by the SBEEA. In short, it cannot be said convincingly that disqualification is operating in line with its underlying objectives. In reality, the number of disqualifications each year is relatively low. In part, this has been caused by significant administrative failings, and IS resource constraints. However, even where directors are disqualified, the overall direct protective

---

[287] 3.24.
[288] ibid.

benefit of disqualification proper to creditors is limited. This may be set to change following the introduction of the compensation mechanisms, which provide a means of direct redress for creditors. However, as has been alluded to, and as will be more fully expanded upon in the next chapter,[289] the author is sceptical as to its utility given the tiny proportion of directors that are likely to be suitable to pursue. Thus, any real increase felt by creditors is likely to be minimal at best. Returning to disqualification proper, concerns of construction within section 6 have also played their part in diminishing the efficacy of the regime. Put simply, there is little wonder that directors often struggle to understand the extent of their (ever increasing) duties, and the type of conduct that might lead to a finding of 'unfitness'. Whilst it is reassuring that this has been recognised by the state in its enactment of the SBEEA 2015 as being a concern, only time will tell whether the measures put in place go far enough. One of the author's primary concerns, which has been laboured throughout this chapter, is that the deterrence objective continues to go unfulfilled. Much of this stems from a sheer lack of awareness of the sanctions that directors can face should they misbehave whilst carrying out their office. Whilst true rogues will never be dissuaded from misconduct, and can likely never be deterred by sanctions, far more could be done to increase the profile of disqualification in an effort to target the vast majority who *can be deterred* if both the knowledge of, and the threat of, sanctions is pervasive enough. As a corollary to that point, the third objective of disqualification – raising standards of management – exists, in this author's mind, in name only. It has been shown that the state takes no proactive steps to improve standards and appears simply reliant on the deterrent aspect

[289] 3.57.

of disqualification to carry this objective into effect. But, the failure of disqualification as a deterrent has thus inevitably led to failure in equal measure of this objective. The potential scope for oppression in the regime is another area that needs to be monitored carefully, particularly given the introduction of compensation orders and undertakings. It seems to this author that the disqualification regime is rather on the cusp of 'penal' or 'criminal' territory. Care must therefore be taken to prevent the compensation provisions from pushing it over the cliff edge.

3

DISQUALIFICATION UNDERTAKINGS: AN EMPIRICAL STUDY

3.1 Given the large amount of literature on the subject of disqualification undertakings it is surprising that very few studies of an empirical nature have been conducted. In part, this may be a result of statistics published on an annual basis by CH and the IS.[290] As the body responsible for maintaining the statutory register of disqualified directors,[291] the data published by CH provides details as to the total number of directors disqualified each year, whether by order or undertaking. The data is broken down by disqualifications made under each section of the CDDA 1986. The statistics provided by the IS, on the other hand, report details of only those directors that they themselves have investigated and prosecuted. The IS data, however, is far more extensive. It contains details of the total number of directors disqualified each year; a breakdown of disqualifications by period based upon the *Sevenoaks* classification; and,

[290] Each of these agencies produces a report that contains a series of numerical observations about the disqualifications (both orders and undertakings) made over the course of the year. For example, see the 2013 data: IS, *Supporting Data for Comparison of Performance in 2012-2013 to Previous Years* (2013) <http://bit.ly/1iNa5YC> accessed 14 April 2014; CH, *Statistical Tables on Companies Registration Activities 2012-2013* (2013) <http://bit.ly/ 2pTlhBq> accessed 14 April 2017.
[291] CDDA 1986, s 18.

in the case of section 6 CDDA 1986 undertakings, a breakdown of the type or category of allegations of misconduct which led to the disqualification.

3.2 These 'headline' figures, particularly those of the IS, provide some insight into the operation of the regime. In some ways, however, they simply beg more questions than they answer. In pursuit of developing a more nuanced understanding of the undertakings regime, this chapter explores the findings of a survey of disqualified directors conducted by the present author. In gathering individual records of directors and conducting a detailed analysis of the results, the current state of the disqualification undertakings regime will be examined in order to evaluate its adherence to the global aims of disqualification, as set out in the previous chapter.[292]

EXISTING SURVEYS

3.3 Before setting out the approach of this author, some attention should be paid to the existing surveys in this area. There are three of note. The first was carried out by the NAO in 1993,[293] which set out *inter alia* to understand the effectiveness of the disqualification regime.[294] Some of those findings were discussed in the previous chapter.[295] The second was conducted by Hicks in 1998.[296] This empirical analysis considered disqualification orders and their wider impact, and in doing so sought to assess the effectiveness of disqualification as an enforcement mechanism. The third, far more recent, survey was conducted by Williams in 2008 and published in 2011.[297] It

[292] 2.5
[293] NAO Report (n 124).
[294] Though it should be noted that both of these reports, of course, pre-dated undertakings.
[295] 2.12.
[296] Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18).
[297] Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18).

analysed 397 records of directors disqualified by undertakings. The existence of other statistical material allows for some direct comparison between findings across the various sources, assuming a similar methodological approach. To that end, the author will take a similar approach to that of Williams in his analysis. However, this chapter intends to bring those statistical findings up to date and take Williams' research one-step further in order to provide yet additional insight as to the effectiveness of the current regime. It will do so largely through the involvement of a second data source, namely the register of disqualified directors provided by CH.

PURPOSE OF THE SURVEY

3.4 The primary purpose of the survey is to uncover, as accurately as is possible, whether the current undertakings regime operates as it ought to. It is suggested here that an effective, and thus successful, undertakings regime should ensure that directors are appropriately being disqualified within the meaning of section 6 CDDA 1986; for a period of time that is both adequate to protect the public, and proportionate to the misconduct committed; that the disqualification regime acts as a deterrent to others from committing misconduct; and that the consequences of breaching an undertaking are of gravity such as to dissuade disqualified directors from doing so, thereby raising standards. Ultimately, with this in mind, such a regime should facilitate the protection of the public against delinquent company directors. The author sets out to:

(a) demonstrate that the survey data is sufficiently valid and reliable for present purposes;

(b) explore the issues and defects that arise in the data sources used;

(c) assess the accuracy and utility of the online register of disqualified persons provided by CH;

(d) demonstrate the most common forms of misconduct that lead to disqualification for 'unfitness', as well as the average period of disqualification for each such category, and therefore the forms of misconduct which attract both the highest and lowest periods of disqualification. Moreover, to speculate upon the process that the IS undertakes in determining the period of disqualification, and any relevant factors that may be considered as part of that process;

(e) consider the average deficit of an insolvent company which led to a director being disqualified;

(f) explore the deterrence implications of disqualification by identifying those directors that act in breach of pre-existing disqualifications or bankruptcy restrictions;

(g) consider the potential implications of compensation orders and undertakings on the regime going forward; including the 'target market' for them based upon an analysis of the solvency of disqualified directors;

(h) analyse the share capital of those insolvent companies that led to a director being disqualified, so as to comment on the issue of capitalisation; and

(i) assess the number of disqualified individuals that directed owner-managed companies.

METHODOLOGY

The Data

3.5 The source of the data, which forms the basis for much of the statistical analysis presented hereafter, was the Disqualification Outcomes Facility provided by the IS (the 'IES').[298] The IES is, in effect, a publicly available register of disqualified directors.[299] Part of the reason for its existence is to demonstrate the success of IS enforcement agents - adding to the deterrence effect – and, as such, a new record is listed on it when an undertaking is obtained. Records remain live for a period of three months from the date that they are first added.[300] Each record contains a large amount of biographical

[298] IS, Disqualification Outcomes Facility <http://bit.ly/2u2VWq7> accessed 14 April 2014.
[299] Though it should not be confused with the statutory register maintained by CH; the IS have no statutory obligations, as far as the author is aware to maintain (or even provide) the IES.
[300] IS, 'Disqualified Directors Search' <http://bit.ly/1eEx9GH> accessed 14 April 2014. It should be noted that the IES provides three-months of data following the date of submission to the database; not from when the undertaking started. The date of submission is generally several weeks later.

information about each director including their name, last known address, date of birth and nationality. It also contains details of the insolvent company, the length of the disqualification and its start and end dates. Importantly, within each record is also a detailed report of the director's misconduct which led to the disqualification. This report is adapted from the undisputed findings in the 'Schedule of Unfit Conduct' that is appended to every disqualification undertaking. As will be discussed, this misconduct report generally is made up of certain 'stock' phrases. In many cases it also includes details of the insolvent company's assets and liabilities, as well as any creditor deficiencies at the time of disqualification.

3.6 *The period of the survey* The author collected data from the IES for analysis on the 30th November 2013. On that day, there were 288 records listed. Given the stated three-month viewing period from the date of submission, this should have dictated that undertakings added between 30th August 2013 and 30th November 2013 were visible. However, the data in the survey actually spanned across an approximately four-month period from 29th July 2013 to 19th November 2013. In contrast, Williams in his survey was afforded six months of data from the same source.[301] Whilst something of a minor point, the author conducted some investigations to explore the reduction (by approximately half) of the data made available. It is proven through the use of Internet archiving tools that six months of data was available on the IES until approximately July 2011.[302] At the same time the IS website was overhauled as part of a government initiative, as commented upon in the Annual Report for that year:

---

[301] Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 5.3.

[302] This was achieved using the Internet Archive 'Wayback Machine' at <http://bit.ly/1i7Bzdj> accessed 1 July 2017.

> At the end of July 2011, The [Insolvency] Service's website was transferred to the BIS website platform. The transfer was part of the government's Service Transformation Agreement which set out to improve delivery by radically reducing the number of government websites by 2011.[303]

It is unclear why the decision was taken by the IS to reduce the time period for which records are displayed. However, it is suggested that in doing so the IS has, despite its mandate to improve the delivery of services, surely hindered the public interest aspect of ensuring the information it publishes is freely available to interested parties. Not only did the transfer to the DBIS platform see a reduction in the number of records visible at any one time, it also significantly altered the format and type of the data presented. Before the redesign, the IES contained a greater number of variables within each record, including a figure of the deficiency of the company; type of insolvency; sector or business the company was involved in; whether the disqualification was the result of an order or an undertaking; and the date the order was made or the undertaking was given. In the present database, most of this supplementary information was available within the misconduct details section of each record, though each report had to be individually read and analysed to extract the requisite information. As such the IES has clearly seen a decrease in both functionality and usability between the time of Williams' survey and the one conducted by the present author. In the case of the additional details within each record, this can likely be put down to resource constraints.[304] However, there appears to be no conceivable explanation for reducing the number of records placed on the system. Nonetheless, save for the reduced scope, this did not affect the substance of the survey carried out.

---

[303] IS, *Annual Report and Accounts 2011-2012* (2012) <http://bit.ly/2tsQOdx> accessed 30 April 2016, 27.

[304] It is likely that a similar exercise would have to be undertaken by IS staff to complete each record at the point of data entry; a lengthy (and costly) process.

3.7 *Collecting the Data* The IES is simply a list on a single webpage of every director available to view at the particular time of access.[305] Summary details were provided for each director on this page including the full name, company name, disqualification length, the date of submission to the database, and a hyperlink allowing the user to click through to see 'more details' about a particular record. This 'more details' webpage included the record of misconduct detailed previously. A computer programme was written by the author for the purpose of automatically retrieving all of this data, including that set out on the 'more details' page. This approach was adopted given the author's background in computer science and in order to reduce the time taken to complete the study. Otherwise, collection would have been a very protracted and laborious process. Upon retrieving the data, the programme collated it into a single, keyed, table within a relational database both for ease of viewing, and so that statistical analysis could be conducted at a later point in time using the application *SPSS Statistics* ('SPSS').[306] Table 1 below indicates the table structure of the data obtained by the author's programme:

[305] IS, Disqualification Outcomes Facility <http://bit.ly/2u2VWq7> accessed 14 April 2014.
[306] IBM Corporation, *IBM SPSS Statistics for Macintosh,* Version 21.0 (Armonk, NY: IBM Corporation, Released 2012)

Table 1: The structure of the table containing data from the IES Database

Name	**Description**
id	A unique integer identifier (primary key)
name	The name of the director disqualified
co_number	The number at CH of the company involved
co_name	The name of the company involved
length	The period in the format 'X Years Y Months'
submitted	The date the record was added to the IES
dob	The date of birth of the director involved
date_starts	The start date of the disqualification
conduct	The misconduct report

3.8 *Data Processing* Once the data had been collected, processing was required to make it compliant for import into SPSS. In three cases a record suffered from a broken 'more details' link. Because of this, two of the three records in question could not be included in the survey data due to the fact that the vital information relating to the misconduct could not be sourced. However, the third of these records *could* be included as the individual in question was one of two directors disqualified due to their misconduct in the management of the same company. Moreover, each suffered the same period of disqualification. On that basis, it was assumed for the purposes of the survey the conduct leading to disqualification for one director (which *was* available for viewing) was the same for the other (which was not). In addition, one of the records in the database was a duplicate and so was removed. For technical reasons, namely to enable numerical processing, it was also necessary to convert the data in each 'length' field (containing the period of disqualification) from a string type (e.g. '12 Years 6 Months') to a decimal floating-point type variable (e.g. 12.5). Overall, counting the exclusions and corrections, this left a total of 285 records to be used for analysis in the survey.

Limitations, reliability and validity

3.9 *Introducing the DDR* At this stage it is necessary to introduce a second database used by the author in conducting the survey: the Disqualified Directors Register ('DDR') provided by CH.[307] As the name would suggest, this contains a list of every[308] disqualified director. It is this register that CH is required to maintain by statute in the public interest. Much of the same biographical data provided by the IES is also available on the DDR. Moreover, it contains basic details about the company or companies involved; the length of the disqualification; the start and end dates of the disqualification; the section of the CDDA 1986 (or CDDO for Northern Ireland) under which the individual was disqualified; and the number of disqualification orders against the individual[309]. Information on the DDR is viewable publically until the disqualification lapses at which point it is, presumably automatically, removed. What the DDR does not provide, unlike the IES, is the misconduct report itself. Instead, it merely documents the authority under which the disqualification was made, for example, 'CDDA 1986 S7'. It is therefore impossible from this dataset alone to ascertain the underlying factual background to the misconduct.[310] The initial data from the DDR was retrieved on the same day as that of the IES, at which point there were 7,874 disqualified directors on the register. The DDR was put to a variety of uses, and it will be revisited throughout this chapter and the thesis. However, it must be

[307] CH, Disqualified Directors Register <http://bit.ly/1oRmuiu> accessed 14 April 2014. It is expected that this hyperlink will cease to function in the near future as CH rolls out the new version of its register (currently in beta testing). For the new register see <http://bit.ly/2sYmUKt> accessed 1 July 2017.

[308] Though, as will be demonstrated later in this chapter, the statutory register is incomplete. See 3.50.

[309] It is of course possible to have concurrent disqualifications orders or undertakings made against a director: CDDA 1986, ss 1(3) and 1A(3).

[310] This will be set out later in the chapter as a criticism of the current state of the online register. See 3.50

introduced at this stage as in large part it was used as a way of investigating the reliability and validity of the survey data. It is remembered that when the SS accepts an undertaking prosecuted by the IS, the information is added to the IES as record of the disqualification. This information is then forwarded to CH for publication on the DDR. Similarly, when a disqualification order is made by a court there is an obligation to forward details of the order directly to CH for reflection on the DDR.[311] Each record on the IES *should* therefore appear on the DDR, and contain the same data.[312] This fact allowed the author to cross-reference the two data sources so as to make findings on the survey data's integrity overall.

3.10 *Errors and omissions* It is suggested that most would have no reason to be in doubt of the accuracy of government data. Indeed, prior academic works, also predicated upon the validity of the official data simply assume accuracy without question.[313] Following the collection of the survey data, and having had the benefit of the DDR however, the present author is less convinced. On that basis, the limitations of the survey must now be dealt with. Due to the fact that the survey is in effect made up of secondary data the findings made – and the conclusions drawn – assume that the data is both reliable and valid. This assumption underpins all that is to follow. Whilst collating the data the author carried out several tests to ensure data consistency and validity. Checks were made so as to ensure that there were no obvious errors or

[311] The Companies (Disqualification Orders) Regulations 2009, SI 2009/2471 reg 6. However, it has been suggested in the past that this does not happen in a timely fashion, leading to inaccuracies on the register. This point, amongst others, will be discussed later in this chapter, see 3.50.
[312] At least, of course, in so far as the data is held on each respective system. As is implied, they often do not match: see 3.50.
[313] By way of example, Williams when conducting his survey dealt with the matter in a sentence; indicating that there was no reason to doubt the data provided. See Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 5.70.

omissions in any of the records before conducting the statistical analysis. It transpired that there were six omissions and six errors,[314] as detailed in Figure 1 below:

Figure 1: Errors and omissions in the survey data

ERRORS			
Field	**Raw Value**	**Rectified Value**	**Description**
dob	19/07/2013	19/07/1956	Human error. The current year was entered instead of the year of birth. Correct data obtained from DDR.
	28/03/2013	28/03/1956	Human error. The current year was entered instead of the year of birth. Correct data obtained from DDR.
	02/11/1969	01/11/1968	Human error. The date of birth was incorrect. Correct data obtained from DDR.
date_starts	2103	2013	Human error. A typographical was made inputting the current year.
submitted	213	2013	
	22/08/2008	22/08/2013	Human error. The incorrect year of submission was entered.

[314] Included within that total are the three previously mentioned records; two excluded and 1 rectified.

OMISSIONS		
Field	**Rectified Value**	**Description**
submitted	N/A	The submission date was blank. This record could not be rectified, though this particular column is not consequential to the findings of the survey.
	N/A	The submission date was blank. This record could not be rectified, though this particular column is not consequential to the findings of the survey.
dob	06/11/1960	The date of birth was blank. Cross-referencing the name and company number with the DDR rectified this.
conduct	N/A	The 'more details' link to this record was broken and therefore the conduct data could not be established. This record had to be removed from the survey entirely.
	N/A	The 'more details' link to this record was broken and therefore the conduct data could not be established. This record had to be removed from the survey entirely.
	N/A	The 'more details' link to this record was broken. Conduct data was obtained from another director of the same company and the record was rectified.

3.11 At this juncture, the impact of these errors and omissions upon the integrity of the survey demands further comment. Many were identified with a cursory reading of the data gathered, and others were confirmed by cross-checking the information with the DDR. The reader must be reminded that the IES is not the official public register and, as such, one might expect there to be less thorough quality control standards applied in ensuring the integrity of the data in respect of that database. After all, these are tasks of administration and are susceptible to human error. In the context of the survey these errors and omissions accounted for just less than 5 per cent of the records. However, it should be recognised that a seemingly small and controlled amount of human error can give rise to catastrophic consequences in a statistical survey.[315] In order to address and minimise data entry issues the author used the two databases at hand, having the benefit that they covered largely the same information; but were from two separate executive agencies. As a result, many of the records in issue could be rectified quickly before importation into SPSS. In the case of the errors, the evidence strongly would suggest that simple human error is at fault. It is more difficult to speculate upon the reasoning for the omissions in the survey data. However, it is likely that the information was not on hand at the time of the data input, or there was an oversight on the part of the one responsible for the entry.

3.12 *Summary* Given the above findings it is clear that although there were some issues with the data, the rate of error would appear to fall within 'acceptable' margins.[316] It should also be noted, however, that the error rate stated is only calculated upon findings following basic validation tests. It is therefore anticipated that the rate of error

[315] As stated by Barchard and Pace, '[j]ust one or two serious data entry errors can completely alter (and invalidate) a statistical analysis'. See Kimberly Barchard and Larry Pace, 'Preventing human error: The impact of data entry methods on data accuracy and statistical results' (2011) 27 Computers in Human Behavior 1834.
[316] See Ian Atkinson, 'Accuracy of data transfer: double data entry and estimating levels of error' (2012) 21 Journal of Clinical Nursing 2730, 2731 where data entry error in that survey was posited at between 2.3 and 26.9 per cent; though standard rates of expected error depend largely on the type of data entry method used: ibid 1836.

may in fact be higher, and the potential for error must be identified as a limitation of the analysis set out hereafter. Aside from those records mentioned, cross-referencing between the IES and DDR showed no signs of inaccurate reporting of the basic biographical data,[317] nor the period of disqualification, for those records that appeared in the DDR. As will be explored later in this chapter, however, not all records were available on the DDR for verification of the IES data and as such these were impossible to verify against a second source.[318] Verification of the misconduct reports was impossible for present purposes,[319] and as such it is an assumption of the survey that they were both correct in content and in their association with each individual record. Naturally, all of the above is predicated on the global assumption that at least *one* of the databases used in the survey was accurate; the likelihood of which is not in question for the present purposes, though it must be identified as a potential limitation. The author has minimised his own data entry error culpability by ensuring that the data was retrieved, and imported into SPSS, by automated means and not manually. Save for correcting the data as set out in Figure 1 above, no further modifications were made.

Analysis

3.13 With the data collated, corrected, and imported into SPSS the next phase was to carry out the survey. This section will identify some of the substantive methodological decisions; laying the ground so that the reader can readily comprehend the subsequent findings. As has been stated, the IS provides its own measure of statistics in each annual

[317] Though it should be noted that in Hicks, in his 1998 survey discovered many director addresses on the register were either missing, incomplete, or outdated. See Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 117-118. This was relevant to Hicks' research as he contacted directors by post.
[318] 3.50.
[319] Obtaining copies of original undertakings and their accompanying Schedules was, for present purposes, simply not feasible.

report that is broken down into various categories of misconduct. Table 2 below reproduces IS data from the 2012-2013 annual report and illustrates the number of allegations made across each category of misconduct over five financial years. The data reflects orders and undertakings made solely under section 6 of the CDDA 1986. As is shown, the number of allegations made can be seen to decline over the period, though it averages at around 1500 per year:[320]

Table 2: Disqualification Orders and Undertakings (Section 6 of the CDDA 1986): Allegations Made[321]

	2008-09	**2009-10**	**2010-11**	**2011-12**	**2012-13**
Crown Debts	563	816	636	635	626
Accounting Matters	381	448	342	200	152
Transactions to the detriment of creditors	246	391	392	161	103
Criminal matters	174	258	259	102	54
Misappropriation of assets	49	68	59	56	28
Technical matters – statutory obligations	46	33	70	52	50
Trading at a time when company knowingly or unknowingly insolvent	44	40	35	7	1
Phoenix companies or multiple failures	14	12	7	2	0
Other	0	98	0	0	0
Total	*1517*	*2164*	*1800*	*1215*	*1014*

[320] Though since the time of the survey, the figures do appear to be increasing once more. For the year 2016-2017, 1272 allegations were made: IS, *Insolvency Service Enforcement Outcomes 2016-17* (n 87).
[321] IS, *Supporting Data for Comparison of Performance in 2012-2013 to Previous Years* (n 290) 3.

3.14 The author adopted these categories in his own survey. More needs to be said as to how these categories of allegations are determined. The misconduct report accompanying each survey record consisted of 'stock' phrases, i.e. specific phrases that were systematically used across the reports to identify particular types of misconduct. It should be noted that these 'stock' phrases formed the bulk of the report. Precisely zero of the records in the survey made reference to companies or insolvency legislation. The lack of primary legislation being cited is somewhat surprising, though this may be for several reasons; the most obvious perhaps being a desire to express the undisputed conduct in plain English so that it is understandable by the wider public when placed on the register.[322] The use of 'stock' phrases however permitted the author the means to easily sort and categorise the type of misconduct within each record. Not by coincidence, the 'stock' phrases also fell into the broad categories listed in the IS annual report (e.g. Crown debt). It is obvious then that the misconduct report, given that it permits a 'drilling down' into more precise reasons for the disqualification, allows for a considerably greater scope of analysis than that found in the official statistics. An example of a 'Crown debt' misconduct report, with 'stock' phrase emphasised, is set out below:

> '[The director] failed to ensure XYZ Limited complied with its statutory obligations to submit Value Added Tax returns and make full payment to HMRC. By failing to make the requisite payments for VAT when they were due, *XYZ traded to the detriment of HMRC.'*

3.15 It must be stressed to avoid confusion in the ensuing analysis that the number of allegations made, as is shown in the IS annual report, is <u>not the same</u> as the number of directors disqualified. This is because it is possible that an individual director has

[322] As well as, of course, the director himself before he signs it.

accepted an undertaking concerning multiple allegations of misconduct. In short, a director may be disqualified for more than one reason. As such, the number of allegations generally exceeds the number of actual disqualifications made. For example it is fairly common, as will be seen from the survey data, for a director to accept an undertaking on a 'Crown debt' basis, and simultaneously on a 'accounting matters' basis.[323] In the IS data, this would then lead to one instance of misconduct being counted for each of these categories. It is important to identify this as in conducting the author's own survey the same approach was taken. For the sake of comparison between the IS data and the present survey, it was also desirable to collate the data relating to the misconduct description into *similar* broad categories as the ones provided by the IS in its annual report.[324] It should be noted that the precise methodology of how the IS data is collated and categorised was not published as at the time of conducting the survey.[325] As such it was not definitively known which 'stock' statements fell within the broader categories and therefore a *direct* comparison of the two is difficult.[326] However, the author in collating the survey data into his own categories took a common-sense approach.[327]

---

[323] The reader will appreciate that the reason for this is that they are linked. Generally speaking accounting failures will often mean that a person is not properly paying HMRC. In terms of the 'stock' statements which led to these categorisations, it was very common for a report to cite that a director 'failed to maintain and/or preserve and/or deliver accounting records' ('accounting matters') which then led to a 'breach of obligations to HMRC' ('Crown debts').

[324] A measure that was also adopted by Williams throughout his survey: Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 5.8, Figure 1.

[325] This has since changed. See: IS, 'Guide to Insolvency Service Enforcement Outcomes' (2015) <http://bit.ly/2tXg6Rx> accessed 1 June 2017.

[326] For instance, the category 'Other' is one that is especially difficult to anticipate with any accuracy what particular types of misconduct might be included.

[327] To give a simple example, any 'stock' statements which mentioned a form of detriment to HMRC, howsoever caused, were categorised as Crown debts. Though, as with any rule there is an exception: MTIC fraud was not included in the Crown debt category as explored below. See 3.36.

3.16 As there were multiple 'stock' statements that fell within many of the broader categories it was very common for multiple allegations within the same category to be made. For instance, in relation to Crown debts three different 'stock' statements were identified:

(a) trading to the detriment of HMRC;

(b) breach of obligations to HMRC;

(c) transaction(s) to the detriment of HMRC.

It often (though not always) transpired that a director disqualified on the basis of Crown debts would have 'breached her obligations to HMRC' and ultimately 'traded to HMRC's detriment'. This would lead to two allegations being registered against the director, though within the same broad category of Crown debts. As such, in order to output meaningful data where there were multiple 'stock' statements within a broader category, the number of unique records within that category was also calculated so it could be compared to the total number of records in the survey.

FINDINGS

3.17 With that said, the findings of the survey will now be explored. Figure 2 below shows the breakdown of the survey data; categorised in the fashion explained previously:

Figure 2: Survey Data: Disqualification Orders and Undertakings (Section 6 of the CDDA 1986): Allegation Types

Misconduct description		Allegations	Category (%)	Total (%)
Crown Debt		**175**		61.4
	Trading to the detriment of HMRC	163	62.5	57.2
	Breach of obligations to HMRC	96	36.8	33.7
	Transaction(s) to the detriment of HMRC	2	0.8	0.7
Accounting		**53**		18.6
	Failure to maintain and/or preserve and/or deliver accounting records	39	71.0	13.7
	Failure to produce and/or maintain accounting records	4	7.3	1.4
	Failure to prepare accounting records	1	1.8	0.4
	Failure to deliver accounting records	3	5.5	1.1
	Failure to file accounts and/or returns	5	9.1	1.8
	Overvaluation of asset to artificially inflate company value	3	5.5	1.1
Detriment to creditors other than the Crown		**68**		23.9
	Insolvent trading	32	33.3	11.2
	Misappropriation/diversion of assets	55	57.3	19.3
	Transaction(s) at an undervalue	9	9.4	3.2
Pre-existing disqualification		**11**		3.9
	Acting as a director whilst disqualified	4	36.4	1.4
	Allowing a director to act whilst knowing that they were disqualified	2	18.2	0.7
	Acting as a director whilst an undischarged bankrupt	5	45.5	1.8
In dealing with suppliers and/or customers		4		1.4
Missing Trade Intra Community (MTIC) VAT Fraud		9		3.2
Breach of fiduciary duties		42		14.7
Failing to cooperate with a liquidator		4		1.4
Breach of technical statutory provisions		23		8.1
Other		14		4.9

3.18 The emboldened and underlined figures represent the number of unique records within each category that contained multiple 'stock' allegation statements, as previously explained. In addition to the breakdown of allegations above, the periods of disqualification based on *Sevenoaks* brackets are displayed in Table 3 below. The mean average period of disqualification in the survey was towards the lower extreme of the middle *Sevenoaks* bracket; 5.50 years. As is shown below, the vast majority fell within the lowest bracket. In Williams' survey the average period of disqualification was 5.73 years.[328] A comparison between the two therefore indicates a decrease in the number of middle bracket disqualifications since 2008, with the majority being redistributed to the lowest bracket.[329]

Table 3: The periods of disqualification in undertaking cases across the three data sets

Survey	**Length (percentage of total)**			**Total**
	1-5 years	*6-10 years*	*11-15 years*	**Cases**
Archer (2013)	183 (64.2)	75 (26.3)	27 (9.5)	285
IS (2012-13)	633 (61.4)	287 (27.8)	111 (10.8)	1031
Williams (2008)	224 (56.4)	127 (32.0)	46 (11.6)	397

Preliminary Observations

3.19 Whilst the table of misconduct will be dealt with in much more detail throughout the course of this chapter, some preliminary observations will be made at this stage. The three categories that attract the most allegations are:

(a) Crown debt misconduct

(b) Accounting misconduct

(c) Transaction(s) to the detriment of creditors (other than the Crown)

[328] Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 5.10.
[329] The IS data for 2012-13 shows an average of 5.7 years (5.4 for undertakings; 7.0 for orders). See IS, *Supporting Data for Comparison of Performance in 2012-2013 to Previous Years* (n 290). The latest IS data as at 2016-2017 indicates a marginal increase at 5.8 years (5.5 for undertakings; 7.5 for orders). See IS, *Insolvency Service Enforcement Outcomes 2016-17* (n 87).

By way of comparison, for the year 2012-2013 the IS reported 61.7 per cent of allegations made involved Crown debt (61.4 per cent in the present survey). In relation to accounting matters, the IS statistics state 15.0 per cent of total cases, as opposed to 18.6 per cent in the present survey. Finally, the IS statistics in relation to transactions to the detriment of other creditors was 10.2 per cent, compared a more considerable 23.9 per cent in the author's survey.[330] On the whole, survey data fits the trend evidenced within the IS statistics, and those within Williams' survey[331]. It can therefore be said with some confidence that, in terms of the broad categories of misconduct, the types and frequency of misconduct reported have remained fairly constant between 2008 and 2013. The remainder of this chapter, then, will go on to consider each category[332] in significantly more detail to unearth how the undertakings system operates in practice. Ultimately, with a focus on gauging the overall effectiveness of it.

Crown Debts

3.20 *What are Crown debts?* Much confusion in the jurisprudence has emerged in relation to so-called 'Crown debts' over time. So much so that it led Dillon LJ in *Sevenoaks* to describe them as a 'term of art'[333]. It is a term that, in this context, has been used to describe debts owed by a company to the HMRC in respect of NIC, PAYE and VAT; though not generally debts in respect of other matters. Following the introduction

---

[330] IS, *Supporting Data for Comparison of Performance in 2012-2013 to Previous Years,* (n 290). The reason for the small discrepancies may be methodological.

[331] Williams' also exhibits similar findings: Crown debts (60.9 per cent); accounting misconduct (29.7 per cent); and transactions to the detriment of creditors (17.2 per cent). See Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 5.8, Figure 1.

[332] The author will, however, not deal with the categories marked other; breach of technical statutory provisions; failing to cooperate with a liquidator; or misconduct in dealing with suppliers or customers in any great depth. This is simply on the basis that these categories added little additional value to the survey findings on the whole.

[333] *Re Sevenoaks Stationers (Retail) Ltd* [1991] Ch 164 (CA), 175.

of the CDDA 1986, the courts were long plagued by a number of questions in relation to the significance of debts owed to HMRC. Predominantly, these questions revolved around the circumstances in which non-payment of Crown debts can render a director liable to a finding of 'unfitness', and whether Crown debts are to be treated differently (i.e. more seriously) to debts owed to other trade creditors in the context of determining the period of disqualification. A complete exposition is not desirable here[334], though it should be noted that those questions have since been resolved by the courts.[335] Of course, the assumption must be made, in respect of undertakings, that the SS follows the same approach as the judiciary. Turning to the law, the authorities have made clear, since *Re Verby Print for Advertising Ltd,*[336] that Crown debts are not to be treated differently, in terms of their seriousness or status, from debts owed to other trade creditors in relation to a finding of unfitness. There is no practical distinction. Moreover, in order for a finding of unfitness to be made, simple non-payment is generally insufficient;[337] as is a merely preferring other creditors to the Crown.[338] There must, instead, be a *policy* of unfair discrimination exacted against the Crown in its capacity as creditor of the company.[339]

3.21 *Survey findings* Out of the total of 285 records 175 (61.4 per cent) involved Crown debt, thus it was the most commonly cited allegation by some margin. The misconduct data as embodied in the 'stock' statements (Figure 2 above), largely

---

[334] For a detailed descriptive account of the case law in the area see: Walters and Davis-White (n 77) paras 5-1 – 5-30.
[335] For commentary on the key authority of *Re Sevenoaks Stationers (Retail) Ltd* [1991] Ch 164 (CA) on this issue see: Sally Wheeler, '*Re Sevenoaks* – continuing the search for principle' (1990) IL&P 174.
[336] [1998] BCC 652.
[337] *Re Sevenoaks Stationers (Retail) Ltd* [1991] Ch. 164 (CA), 182-183.
[338] *Re Verby Print for Advertising Ltd* [1998] BCC 652, 665.
[339] ibid 665.

consisted of individuals who traded to the detriment of HMRC (62.5 per cent of Crown debt records). Other misconduct included a breach of statutory obligations towards HMRC (36.8 per cent of Crown debt records).

3.22 *Remembering the rationale* Interestingly, 108 of the total survey records (37.9 per cent) involved misconduct solely relating to Crown debt. The rather elementary analysis set out thus far therefore already raises questions as to whether the original aims of disqualification are reflected in practice. The reader is reminded of the primary aim being to protect the public against abuses of limited liability.[340] The survey data paints a different picture, where a significant majority of directors are disqualified for misconduct connected with being a debtor to the state. It might be argued that the Crown is, by extension, the 'public' in that it is the tax collector for society at large, and as such the objective is being achieved. However, the reality of disqualification as being a champion for the unsecured trade creditor, then, as will be dealt with in due course, is open to considerable challenge. Even more striking is that in nearly two-fifths of all disqualifications in the survey, Crown debt misconduct was cited *exclusively* as the reason for the finding of unfitness. In other words, the figures demonstrate clearly that a significant majority of overall disqualifications contain some element of Crown debt, and a substantial proportion arise solely as a result of Crown debt misconduct. Given HMRC's status as the largest UK creditor[341] this might be explained away by simple statistical probability. By definition, the Crown is a creditor to every trading corporation. As such, in an insolvency setting, it would not be surprising that HMRC is

[340] 2.5
[341] Peter Bailey, 'Insolvency Service Consults on Insolvency Practitioner Fees and IP Regulation' (2014) 349 SMCLN 1, 2.

left unpaid in greater frequency than, say, when compared with other trade creditors.[342] That notwithstanding, it is clear to the author that Crown debts are the lifeblood of disqualification and, when considering its objectives, this is somewhat concerning.

3.23 *A different type of 'cherry picking'* In considering the effectiveness of disqualification, it is crucial to consider who is targeted by the regime. This is because it is fundamental to ensuring that the public are protected that the *right* people are disqualified, and for a length of time proportionate to the misconduct. The IS however, being a government agency, is target driven. It is obvious to any reader of the IS annual reports that the effectiveness of the Disqualifications Unit is judged based upon the number of disqualifications achieved in any particular year, and the time taken for those proceedings to be concluded.[343] In other words, the IS are under considerable pressure to meet (and exceed) these targets. It must also be remembered that the IS do not have an infinite number of resources to pursue suspected director misconduct.[344] On the IS criteria, as disqualifications rise the statistics become more and more attractive politically. However, this is surely a crude method of determining success. Simply increasing the number of disqualifications per year is of little value in terms of the effectiveness of the overall regime, as measured against its objectives to protect the

---

[342] This is compounded by the fact that the Crown faces substantial difficulties in pressing for payment as compared with other trade creditors. See Dillon LJ: *Re Sevenoaks Stationers (Retail) Ltd* [1991] Ch. 164 (CA), 182-183; and generally: Walters and Davis-White (n 77) para 5-29.

[343] For the first time in 2012-2013 the Insolvency Service created a new target relating to the percentage of 'appropriate disqualification cases in which proceedings are instigated in under 23 months'. See IS, *Annual Report and Accounts 2012-2013* (2013) <http://bit.ly/1qxxDFF> accessed 30 April 2014, 13-15. According to Hicks, it was ultimately the NAO's 1993 report that created pressure on the IS to increase numbers: Hicks, 'Director disqualification – the National Audit Office follows up' (1999) 15(4) IL&P 113, 114.

[344] 2.25

public and deter misconduct, if they are improperly targeted.[345] In short, to be effective disqualifications must first and foremost be of *quality*, not *quantity*.[346] This was a point picked up by Hicks as early as 1999.[347] Hicks also made the point that many disqualifications are of sleeping partners, inactive spouses, or other 'sundry nominees'.[348] Whilst these further bolster the statistics, he argues, they do not necessarily address the underlying issue of the abuse of limited liability, nor protect unsecured creditors.[349] Whilst the author has not carried out any statistical analysis to prove or disprove this argument, it does not seem farfetched.

3.24 Moreover, in this vein, it has been suggested by some cynical commentators, including representatives of R3, that this target-driven environment has led the IS to cherry pick the 'low hanging fruit' that are Crown debt cases for investigation and prosecution.[350] This has the political benefit for the IS of bolstering its statistics by increasing the number of actual disqualifications made, and by reducing the average time taken to prosecute such cases. This effect is achieved because, relatively speaking, Crown debt cases are easy to prove[351]. Given the resourcing constraints and other administrative constraints addressed previously, one does not have to think for very long to come to the view that this position is entirely desirable for the IS.[352] When an IP

---

[345] The number of disqualifications may increase over time given the new three-year period (increased from two) that the SS has to make an application for an order: CDDA 1986, s 7(2).
[346] The author borrows Hicks' phrase here: Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 99.
[347] Hicks, 'Director disqualification – the National Audit Office follows up' (n 343) 114.
[348] ibid.
[349] ibid 113-114.
[350] For example, see R3, 'Directors Disqualification: Room for Improvement' (2011) <http://bit.ly/2tXkQ9Y> accessed 1 January 2017.
[351] Due to a readily available paper trail: *Re Sevenoaks Stationers (Retail) Ltd* [1991] Ch 164 (CA), 182; *Re Verby Print for Advertising Ltd* [1998] BCC 652, 665.
[352] 2.25.

files a conduct report[353] with the IS a grid is used to score each individual case that may warrant investigation.[354] Only cases that exceed a particular threshold score will be investigated. Whilst the specifics behind how the grid operates are unclear, it is not a great leap to suggest that it would lend itself to outputting those cases which, based upon the type of suspected misconduct, are capable of being successfully pursued within the statutory time limit. However, should the cherry-picking approach be the reality it is submitted that this will ultimately transpire to be highly damaging. It is problematic because it creates the mere *illusion* of a successful disqualification regime. There is no suggestion from the commentators, as far as this author can tell, that directors are improperly being disqualified, i.e. without sufficient evidence.[355] The more likely problem is that where evidence of Crown debt misconduct is uncovered the IS concludes the investigation and looks no further. This, as Williams notes, prevents a 'detailed investigation of a director's conduct revealing a broader unfitness'.[356] Again, it is understandable, though not condonable, why this approach might be desirable for the IS.[357] The danger is that once the minimum threshold for a successful disqualification (on a Crown debt basis) is passed, investigations which may reveal more serious forms of misconduct cease due to the difficulties and costs associated with investigating more complex types of misconduct. Such an approach undermines the objectives of the disqualification regime on two fronts. Firstly, it does not protect the public adequately, as the director is disqualified for a shorter period of time than she otherwise would have

[353] 2.42.
[354] DBIS Committee (n 103) Q129.
[355] Though, as discussed earlier, given the financial pressure placed on directors when considering whether to accept an undertaking, it is of course a danger that this could be exploited: 2.47.
[356] Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 5.14.
[357] 2.21.

been had the further misconduct been uncovered. Secondly, she is not deterred by the threat of disqualification because, in effect, she 'gets away' with the substantive misconduct and faces no consequences for it. It goes without saying that it is not acceptable, because of bureaucratic concerns, that those deserving of disqualification should go unnoticed, or worse, are not pursued (or fully pursued) in order to bolster the statistics. It must be stated very clearly that officials within the IS and DBIS have repeatedly denied this allegation.[358] Moreover, there is no evidence, other than musings by practitioners, that it is the reality. However, when considering the figures presented in this survey, such assurances hardly provide comfort to unsecured trade creditors as to the effectiveness of disqualification. Notwithstanding anything said previously, it is argued that the existence of the cherry-picking argument in the academic and practitioner commentary *in itself* speaks volumes as to the low level of trust and confidence of important stakeholders in the disqualification regime.[359]

3.25 *The period of disqualification* What has not been discussed until now is the period of disqualification solely in respect of Crown debt cases. Table 4 below shows the breakdown as per the *Sevenoaks* brackets:

Table 4: The period of disqualification for Crown Debt cases from the survey

Length (years)	**Total Cases**	**Cases solely involving Crown debts**
2-5	147	101
6-10	26	7
11-15	2	0
Total	*175*	*108*

[358] DBIS Committee (n 103) Q128; DBIS, 'Impact Assessment: Matters to be taken into account by the Court when determining that a person is unfit to act as a company director' (2014) at <http://bit.ly/2uVywQ8> accessed 1 July 2017, 6, fn 2.

[359] A point recognised by DBIS and the IS themselves: DBIS, ibid 6, fn 2.

3.26 Out of the total, 84 per cent of cases fell within the lowest bracket, and the mean average disqualification period within this category was 4.34 years – significantly below the overall mean average of 5.50 years. Where a case solely involved Crown debt, a staggering 93.5 per cent fell into the lowest bracket suggesting that such misconduct, except in the rarest of cases, is only considered 'minor'.[360] There were only two cases that attracted the highest bracket. In the first instance this involved a director who, in addition to his Crown debt misconduct, was found already to have been disqualified. In the other, that director was acting whilst an undischarged bankrupt. Those individuals were given 11 and 12 years respectively.[361]

3.27 *The compensation dimension* When considering the compensation regime, another facet worthy of critique raises its head in respect of Crown debts. Consider the nearly two-fifths of directors in the survey that were disqualified solely on the basis of Crown debts misconduct. Each director within that demographic would, if the legislation were in force at that time, have been exposed to compensation liability.[362] If pursued, any deficit could be awarded solely for the benefit of the Crown, or as a contribution to company assets.[363] First, it should be said that the routine procedure of disqualifying directors who seek to defraud or discriminate against the HMRC is undoubtedly justified. However, it is suggested that it would *not* be desirable should the

[360] This is surprising given the average deficit of companies where misconduct was attributed solely to Crown debt cases was £237,896.45 (median £134,341.50). Evidently, attitudes have changed substantially over time as to the seriousness of Crown debt misconduct. For instance, in the early days it was described as a particularly serious form of 'commercial immorality', see *Re Wedgecraft Ltd* (unreported) 7 March 1986 as quoted in *Re Stanford Services Ltd* (1987) 3 BCC 326, 333.
[361] As will be demonstrated in due course, it seems to be the policy of the SS to make an 'example' of directors who are undeterred by the restrictions made against them. See 3.17.
[362] Only misconduct taking place after 1 October 2015 is able to be targeted for compensation.
[363] CDDA 1986, s 15B. Though where the only creditor is the Crown, as one suspects it probably was in cases where the sole reason for disqualification was Crown debts, the effect is the same.

new legislation engender a practice of pursuing these individuals, for the benefit of the Revenue. Given the large amount of Crown debt cases, there is a real danger the compensation regime will develop to be little more than a state-manufactured tool for the recovery of debts owed to the state. This concern may be lessened somewhat as the IS has stated that it only intends to pursue directors for compensation in the most serious of cases.[364] If seriousness is to be determined by the period of disqualification fixed as set out in the previous chapter, it seems likely that only a small number of Crown debt cases would fall within that category in any case. Until the compensation regime really takes hold, it is impossible to comment upon the approach in reality. However, it is argued here that the purpose of the compensation regime must be the protection of the private creditor. It must not become a backdoor or subversive means of recovering Crown debts. One facet that is particularly worrying, as discussed previously, is that there is evidence to suggest that directors may feel pressured by the SS into giving disqualification undertakings.[365] To reiterate the point: it is not a great leap to assume that directors, when faced with mounting costs, may be similarly pressured into giving an accompanying *compensation* undertaking simultaneously.

Transactions to the Detriment of Creditors

3.28 The second most common category of allegation was transactions to the detriment of other creditors. This was generally due to insolvent trading, transactions aimed at defeating particular (or indeed all) creditors, or showing preference to others either whilst insolvent, or whilst trading within the 'twilight zone'. When considering

---

364 DBIS, 'Impact Assessment: Giving the court and Secretary of State (SoS) a power to make a compensatory award against a director' (n 235) 90.

365 Given that it is the SS's practice to pursue costs against directors that challenge undertakings: 2.47.

it is this category of misconduct that goes to the very heart of the rationale of disqualification,[366] and the compensation regime, it is disappointing to see that less than a quarter of disqualifications in the survey arise from it. This may be for many reasons, including evidential difficulties. For instance, proving unfitness will involve protracted investigations that may be stifled by *inter alia* a lack of evidence, difficulties in accessing records, or sheer uncooperative creditors. Moreover, other threshold difficulties may arise. For instance, in the case of insolvent trading, authority makes it clear that attempts to merely trade out of insolvency will be insufficient to find unfitness, unless the prospects of doing so were unreasonable.[367] This balance must be approached carefully, as it would clearly be in error to disqualify a director whose company failed for legitimate commercial reasons. Of course, all of this evidence gathering takes time and costs money. Both are commodities in limited supply at the IS.[368] The statistics reveal that the bulk of cases in this area involved the misappropriation or diversion of company assets to the detriment of creditors (57.3 per cent of allegation in the category). This invariably involved a director syphoning off assets for her own personal gain. In other cases, it involved using company funds to pay off particular creditors, at a preference to others. Unsurprisingly, the most common creditor paid at a preference was the errant director herself in repaying a loan account.

3.29 *The period of disqualification* Table 5 below indicates the breakdown of disqualification periods for this category:

---

[366] 2.10.
[367] In other words, the company must in effect trade 'wrongfully': *Re Cubelock Ltd.* [2001] BCC 523, para 71; *Secretary of State for Trade and Industry v Creegan* [2002] 1 BCLC 99, para 7.
[368] 2.25

Table 5: The period of disqualification for creditor misconduct cases

Length (years)	Total Cases	Cases solely involving creditor misconduct
2-5	47	10
6-10	17	5
11-15	4	1
Total	*68*	*16*

3.30 The mean average period of disqualification was 5.40 years, i.e. more or less in line with the overall mean average across all records. It is interesting to note that this was significantly higher than the mean average period in Crown debt disqualifications (4.34 years). Given what was said earlier in relation to their being no practical distinction between trade and Crown debts, it might have therefore be assumed by extension that the nature of the creditor should have no bearing on the period of disqualification. As such, although the two factors are not necessarily causative, one might have expected the gap between the two average periods to be closer. As was expected, very few cases solely involved creditor related misconduct as there were almost always moneys owed to HMRC in addition. Disturbingly, 69.1 per cent of the disqualifications were made in the lowest bracket of 2-5 years. The reasoning behind this cannot be conclusively be explained, however, it is especially concerning when considering the underlying policy aims of disqualification. Across the whole survey there was one record solely involving creditor misconduct where the director was disqualified for the maximum 15 years. This was a particularly clear-cut case where the director diverted substantial funds, held on behalf of members of the public, from the company (at least £4.1 million) for the purposes of meeting his own personal liabilities.

3.31 In summary, therefore, the figures demonstrate that disqualification is rather ineffective at protecting the private creditor. This is troubling, as it is surely this category of creditor, first and foremost, that disqualification *must* protect to be capable of being labelled successful. After all, it is unsecured creditors that feel the brunt of any abuses of limited liability. Overall figures are extremely low within this category and when disqualifications *are* made, they are for relatively short periods. In the vast majority of cases this type of misconduct is treated as 'minor' in line with the *Sevenoaks* classifications. It is even more shocking this is so when considering the median average of deficit to creditors in cases solely involving this type of misconduct is £488,636. This state of affairs must surely have significant (negative) implications for the trust and confidence that the public place in the regime. Moreover, when considering the secondary aims, it cannot be said that delinquent directors are likely to be deterred from their misconduct for precisely the same reasons; they are unlikely to be caught, and if they are they will be disqualified for a short period of time.

3.32 *The compensation dimension* As with the private enforcement mechanisms considered, at the heart of the public compensation regime is the protection of (unsecured) creditors. However, the present author is sceptical as to how successful the new regime will be in fulfilling this aim. Simply put, there are very few disqualifications in this category and as such there are likely to be even fewer compensation orders or undertakings that are able (or worthwhile)[369] to be pursued.[370] Again, if the IS only choose to pursue those cases involving the most serious misconduct the potential

[369] 3.57.
[370] If the average deficit in this type of case is nearly £500,000, the author is highly sceptical as to how many directors actually pursued would be able to afford to compensate creditors: 3.57.

number of candidates shrinks into insignificance. On that basis, it is argued here that the utility of the compensation regime in respect of protecting private creditors has been grossly overstated.

Accounting Matters

3.33 Accounting matters were the third most commonly cited reason for misconduct in the survey, making up 18.6 per cent of the total cases. Most involved either a company director failing to provide the appointed IP with detailed accounting records of the insolvent company, or persistently failing to file accounts with the registrar.[371] Good accounting practices are key to the successful management of a company and therefore a failure to keep accounting records is, quite rightly, evidence of unfitness for the purposes of section 6 CDDA 1986.[372] It is also contrary to sections 386 and 388 of the CA 2006.[373] However, the misconduct reports on the whole indicate that it is the impediment caused to the IP in exercising the function of her office that is the main driving force behind the finding; not the breach of the statutory obligation *per se*.[374] The 'failure to maintain and/or preserve and/or deliver accounting records' makes up the bulk of this category (71.0 per cent). Though, what also arises from the analysis is that many directors simply refuse to hand over, or conveniently 'cannot' provide, accounting records. In those cases, it seems from the misconduct reports surveyed that the SS makes an inference that the records do not exist (likely for ease). After all, a failure to keep records renders a director equally (if not more) culpable. It is suggested

[371] Note, that this can also lead to disqualification under CDDA 1986, s 3.
[372] CDDA 1986, sch 1.
[373] Though neither of these sections (nor, in fact, any) were mentioned in any of the misconduct reports.
[374] This is likely because the IP can provide direct evidence of the obstruction, thereby making the misconduct somewhat easier to prove.

that whilst poor record keeping is not, taken alone, one of the more serious forms of misconduct dealt with here, it may be a type of 'gateway' misconduct. This is based on the fact that despite accounting for 18.6 per cent of cases, only 24 cases out of the total (8.4 per cent) exclusively concerned accounting misconduct. Therefore, the vast proportion of directors who fail to keep accounting records are also guilty of other (possibly more serious) misconduct. It follows, then, that poor accounting practices should be an indicator to IPs that greater scrutiny into their activities is required at the investigation stage.

Table 6: The period of disqualification for accounting misconduct cases

Length (years)	**Total Cases**	**Cases solely involving accounting misconduct**
2-5	14	5
6-10	33	18
11-15	6	1
Total	*53*	*24*

3.34 *The period of disqualification* Table 6 above shows the breakdown of disqualification periods for individuals whose misconduct involved accounting misconduct. We see a higher than average disqualification period at a mean of 7.0 years per individual. This category of misconduct also sees the largest range in the company deficit at the point of insolvency when compared to any other. Deficits ranged from a mere £1,757 of liability to £9,106,532 with the median figure being £161,136. This suggests that, as perhaps would be expected, accounting malpractice can be seen across a very broad range of companies. Most accounting misconduct fell squarely within the middle *Sevenoaks* bracket. Dishonest practice, for example falsifying accounts, led to a longer period. Given the attitude of the courts and the SS towards fraud, this is to be expected. Indeed, in the one instance solely involving accounting misconduct where the director was placed in the highest bracket (11 years), it was undisputed that he had previously submitted falsified records to CH which showed that the company was profitable, when it was not. The 14 cases that fell within the lowest bracket all concerned a failure to maintain accounting records in micro-businesses.

3.35 The reason for this higher than average period of disqualification is unclear. It is possible, due to the existence (or lack) of a paper trail in accounting matters, that more serious misconduct is easier to unearth. In any case, the author again takes issue with the utility of disqualification given the above analysis. Can it really be said that the public, and importantly the private creditor, is significantly better protected as a result of cracking down on poor accounting practices? As might be inferred from the tone, it is argued here that it is not. Though, admittedly, the evidence suggests that it may provide a 'window' into identifying other forms of misconduct; perhaps leading to a higher period of disqualification. One issue with accounting malpractice, as with Crown debts, is that it invariably arises from ignorance and incompetence; not necessarily a wilful abuse of limited liability. As such, it is argued that this is one area in which education and training is surely the solution. This is a point to be revisited later in this thesis, when considering reform.[375]

Carousel (MTIC) Fraud

3.36 Missing trader intra-community (MTIC) fraud is, in some ways, a specialised type of Crown debt as it relates to the theft of VAT. However, when conducting the survey, it became obvious that MTIC fraud was deserving of its own category. This was for two substantive reasons. Firstly, disqualification involving MTIC allegations

[375] 6.20.

generally involved much higher than average periods of disqualification which would otherwise skew the results for the broader Crown debts category. Secondly, MTIC fraud is also a criminal matter[376] and so the author was hesitant as how exactly to categorise it.[377] As such it was simply separated. Doing so had little impact on the remainder of the survey results as none of the nine directors who were disqualified for MTIC fraud were disqualified for *any other* reason, i.e. they were disqualified solely on the basis of the fraud.[378] This was a fact unique to this particular category. Another fact unique to MTIC fraud is that all of the undertakings given fell within the highest *Sevenoaks* bracket. Six directors were disqualified for 12 years, with the remaining three for 13 years. This reveals two things. Firstly, the SS is particularly determined to send a strong message that those involved with fraud on the taxpayer (as opposed to just trading to the Crown's detriment) will be dealt with severely. This must be the correct approach. It seems to this author that there can be no greater demonstration of 'unfitness' to direct a limited company than the commission of fraud. Secondly, MTIC fraud cases account for one-third of all undertakings in the top bracket. When widened to encompass all types of Crown related misconduct, this rises to two-fifths. A significant proportion of what is deemed to be the most severe misconduct, therefore, is tied to matters affecting the state. When discussing MTIC fraud, Williams concludes that the state occupies a 'prominent role'[379] at the higher end of the spectrum of the disqualification period.

[376] Generally the charge is conspiracy to cheat the public revenue, see: *R v Paul Ward* [2005] EWCA Crim 1926. As such, a court can impose a disqualification order on conviction under CDDA 1986, s 2. However, it can also arise as a s 6 undertakings issue where the company in question becomes insolvent.
[377] Since the survey was conducted the author has learned that the IS *do* include MTIC within Crown debt.
[378] All nine instances of MTIC fraud involved the sale of mobile telecommunications devices.
[379] Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 5.46.

3.37 Therefore, whilst it is obvious that these individuals are deserving of lengthy bans, when considering the purpose of disqualification, it is in another sense still somewhat troubling. This is because it is indicative of a regime operating largely for the protection of the state rather than, say, the private creditor. Such heavy periods of disqualification are no doubt put in place, in part, so as to deter others from committing this type of misconduct. However, the author is of the view that a fraudster is a fraudster. It seems unlikely that any (civil) penalties will be of any deterrent to this type of individual. This may change following the introduction of the compensation regime. MTIC cases invariably involve large sums therefore, if the IS decides to pursue these individuals (assuming they are worth pursuing), the deterrent factor may increase. However, the same issues arise as discussed previously in respect of Crown debts more generally; the temptation for compensation undertakings to be used as a means of state debt recovery, by the backdoor, must be avoided.

Breach of Fiduciary Duties

3.38 The fact that a director had 'breached his fiduciary duties to the company' was reported in 42 cases out of the total (14.7 per cent). It is not an especially noteworthy category, as the misconduct reports obtained did not give any substantive detail as to what led to the breaching of the duty; merely that the duty was breached, and that this was in itself evidence of unfitness.[380] Despite specifically mentioning fiduciary duties (a legal term) there was not one reference to the duties breached as enshrined within sections 171-177 CA 2006, common law duties, or otherwise. What is surprising, is that the reporting of a breach of fiduciary duties was not *much* higher. Clearly many of the

[380] CDDA 1986, sch 1.

instances of Crown debt or accounting cases, on a strict interpretation, would also involve a breach of fiduciary duties. This is perhaps an issue with the methodology used in the IS's reporting of misconduct, and is indicative of an inconsistency in the approach adopted.

Pre-Existing Disqualification

3.39 In 11 records (3.9 per cent) there was an allegation that the director in question had, either acted whilst disqualified;[381] had acted, or was willing to act, on instructions given by another, knowing that they were disqualified;[382] or had acted whilst an undischarged bankrupt.[383] Out of the 11 cases, one disqualification fell within the lowest *Sevenoaks* bracket, five within the middle bracket, and the remaining five within the top bracket. The only instance where an undertaking was given for a period in the lowest bracket (3.5 years) was where a director (who was not disqualified) allowed another director (who was) to act whilst the former knowing that the latter was disqualified. The highest period of disqualification under this category was 12 years. Interestingly, three out of the 11 records (27.3 per cent) were disqualified *solely* on the basis of a pre-existing disqualification or bankruptcy. It is possible, though entirely speculative, that these individuals were caught by the IS following a 'tip off' from a member of the public.[384]

3.40 As one might expect, individuals who were 'repeat offenders' or acted in breach of restrictions were treated severely. This is important from the perspective of

---

[381] CDDA 1986, ss 1 and 1A.
[382] CDDA 1986, s 15(1)(b).
[383] CDDA 1986, s 11.
[384] Originally this would be by way of the IS 'hotline'; now replaced by an online 'Investigations and Enforcement Services Breach Questionnaire' <http://bit.ly/2tsEg5Z> accessed 1 July 2017.

deterrence and upholding trust and confidence in the disqualification regime. However, it is of course questionable as to whether an additional disqualification order or undertaking is a credible threat to those who are willing to act in breach of their initial disqualification. It is clear that the *real* deterrent for such individuals must be the threat of imprisonment following a conviction under section 13 CDDA 1986. Though, evidently, for some 4 per cent of persons, that is still not a credible threat. This could be due to the fact that prosecutions under section 13 CDDA 1986 are not widely publicised; or that those who *are* disqualified are simply unaware that imprisonment is a possibility.[385] Hicks noted that for the years 1991-92 to 1996-97 the number of successful prosecutions were: 83, 66, 67, 54, 78 and 70 respectively.[386] However, these figures include prosecutions made under section 11 CDDA 1986 (undischarged bankrupts) and so are not a reliable indicator as to section 13 proceedings when taken alone. A Freedom of Information request by this author has determined that in recent years, the number of successful prosecutions has diminished quite significantly, in spite of the number of disqualifications increasing since that time. It should be noted by way of limitation, in similar fashion to Hicks' data, the following figures show those individuals convicted of at least one offence under section 13 CDDA 1986. However, they may have been charged and convicted of other offences simultaneously. Naturally this may have therefore had a bearing on whether a custodial sentence was imposed or not.

[385] See Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 127, where only 12 out of 28 (42.9 per cent) disqualified directors seemed to be aware of imprisonment as a sanction for breach of an order.

[386] These statistics used to appear in annual CH reports; though this is no longer the case: ibid 51.

Table 7: Number of successful prosecutions under section 13 CDDA 1986, the number of custodial sentences and if suspended

Year	Convictions	Custodial sentence	Suspended?
2012-2013	25	10	0
2013-2014	31	21	0
2014-2015	24	19	0
2015-2016	21	9	0
2016-2017	12	5	1

Whilst it is not known how many prosecutions were commenced, so that a success rate can be determined, it is readily apparent that the numbers here are small. On average, in just over 50 per cent of cases over the past five financial years a successful prosecution resulted in a custodial sentence. This figure is likely to be inflated, due to the fact that some individuals may have been convicted of other offences (perhaps more deserving of custody). Although more data is needed in this regard to say with certainty, the present author is sceptical as to the potential deterrent effect of section 13 CDDA 1986 given its low utilisation and the roughly one-in-two chance of going to prison *even where convicted*. It is especially troubling that the number of successful prosecutions has declined since the time of Hicks' study, as this author has not encountered any evidence that might suggest the type of behaviour covered by section 13 CDDA 1986 is itself on the decline.[387] This may be a result of resourcing issues which has led to these matters falling somewhat by the wayside.

[387] Though of course it is recognised that an absence of evidence is not evidence of absence.

THE PERIOD OF DISQUALIFICATION

3.41 As a part of the original hypothesis, the author considered it important to understand the potential factors that may influence the period of disqualification. This is a matter of the gravest importance. The length must be balanced between the protection of the public and the imposition on an individual's freedom to manage a company, if it is to be effective. A period of disqualification that is disproportionate to the aims that are sought undermines the success of the regime. A period too harsh is indicative of an intention to punish, rather than to protect.[388] Similarly, a period of disqualification that is too short is unlikely to have sufficient impact upon the individual concerned; but cause significant wastage of public expenditure in the investigation process. However, the exact mechanics used by the IS for determining the length are unknown. The mean average period of disqualification in the survey was 5.50 years – just outside of the lowest *Sevenoaks* bracket. This is partially skewed by the number of MTIC cases that always result in longer periods of disqualification. The median, it is submitted, is the more appropriate measure at 5.0 years. This figure is rather low, considering the minimum period is two years under section 6. In line with the *Sevenoaks* brackets, this would suggest that most misconduct is only considered to be 'minor'. In fact, there is anecdotal evidence that public perception is that disqualification for a period within this bracket is equivalent to no more than a 'slap on the wrist'.[389] It goes without saying that low periods of disqualification are therefore damaging in terms of the trust and confidence in the enforcement regime, and as a deterrent to future

[388] 2.6.

[389] See for example John Willcock, '4,000 Rogue Directors on Loose in UK Companies' *The Independent* (28 October 1996) at <http://ind.pn/2uCfcrO> accessed 3 January 2015.

misconduct. Moreover, the statistics cause reason to doubt the effectiveness of disqualification should it, on the whole, fail to protect the public for an appropriate period of time. With the assistance of the survey data, the following section will consider the impact of the insolvent company's deficit on the period of disqualification.

Company Deficit

3.42 It was hypothesised that the magnitude of the deficit of the company at the time of insolvency would be a significant factor in determining the period of disqualification. However, analysis of the survey data reveals – somewhat surprisingly so – that this is not the case. The deficit was obtained for each company by reading the misconduct report and recording the appropriate figure. By the very nature of the reports, particularly in cases where there was a lack of accounting records, often this figure was an approximation or a 'minimum potential deficit' and so should be looked upon conservatively. For present purposes, however, the information recorded permits the drawing of some general conclusions. Across the survey, the mean average deficit recorded was £475,149.80 and the median average £164,456.00. The large disparity between the two figures was largely due to the various MTIC fraud cases on one end of the spectrum, and trivial accounting matters on the other. The highest recorded deficit was £9,106,532.00 and the lowest recorded (as in 10 cases in total) was nil.

3.43 A correlation co-efficient calculation was carried out in SPSS, across all of the records within the survey, so as to determine the association (if any) between company deficit and the period of disqualification. The calculation identified a *very* weak, but not entirely non-existent, positive correlation between the two variables ($\rho = 0.288$). This suggests that deficit is of limited relevance in determining the period.[390] However, it is possible that one 'advantage' of a large deficit is that it that it is likely to trigger alarm bells for IPs; causing them to conduct more detailed inquiries. This may in itself lead to disqualification, whereas otherwise the director might have slipped through the proverbial net. As was discussed with accounting misconduct, it may be that a particularly large company deficit is a 'gateway' into exploring the entire extent of a director's involvement and culpability, though the statistics are not conclusive in this regard.

3.44 The fact that there is no obvious correlation between deficit and disqualification period, it is argued, is rather staggering; though it is recognised that the two factors are not necessarily causative. However, the perception conveyed is that directors may run up any number of debts, to any number of creditors (even if well into the millions), without particular consequence in terms of the period of their eventual disqualification. Instead, it is *how they do* it that is at issue. The fixing of an appropriate period is one of the key factors that the author suggests is necessary to a successful disqualification regime. It is therefore odd that company deficit does not appear to be a factor. By contrast, in respect of compensation orders and undertakings, it is a requirement that the amount of loss caused is considered as a factor in determining the level of compensation.[391] This, of course, makes perfect sense. However, there is some possibility that, in the future, this element will also make it into determining the period of undertakings more generally. As stated previously, the 'new' Schedule 1 now

---

[390] By way of comparison, in his survey Williams discovered a practically non-existent correlation ($\rho = 0.0351$); Williams, *Disqualification Undertakings: Law, Policy and Practice* (n 18) para 5.11.
[391] CDDA 1986, s 15B(3)(a).

requires in all cases that consideration be given to the 'nature and extent of any loss or harm caused'. Loss can of course include financial loss. This may therefore pave the way for a new process of evaluating periods of disqualification, with harm to creditors playing a more central role. It is argued that tying culpability directly to the extent of the damage caused must represent a better approach.

CAPITALISATION

3.45 It is often stated that the undercapitalisation of limited companies leads to excessive risk taking; increases moral hazards for company directors; and generally lends itself towards the abuse of limited liability.[392] These assertions will be examined in more detail in the penultimate chapter, when discussing the prospect of minimum share capital rules as a measure of reform. However, as part of the survey, the author sought to understand exactly how undercapitalised (if at all) the average company is where it has been driven into insolvency by a director who later is disqualified. The process of doing so was straightforward. The 285 survey records of disqualified directors resulted from a total of 224 insolvent companies.[393] A search on the CH register was carried out for each of these companies in order to determine its share capital based on the last annual return filed, or on the information provided upon incorporation (whichever was the latest available). For 29 of the companies the information was not held, was unavailable or was not applicable[394] to the entity type. As such, 195 companies were able to be surveyed for their share capital. One company had a share capital of 1

[392] 1.6.

[393] This is obviously due to the fact that multiple directors from the same company were disqualified at the same time.

[394] Three companies were limited by guarantee; two were LLPs; and for the others the information simply was not held.

USD, which was treated as 1 GBP for present purposes. A simple frequency table, Table 8, is shown below to illustrate the data:

Table 8: Share capital of companies with disqualified directors

Share capital	Frequency	Percentage (%)	Cumulative (%)
£0-100	156	80.0	80.0
£101-1000	23	11.8	91.8
£1,001-10,000	6	3.1	94.9
£10,001-100,000	6	3.1	97.9
£100,001+	4	2.1	100.0

3.46 It is unsurprising to see that the vast majority of companies featured in the survey had a share capital of less than £1,000, with many choosing common denominations such as £1, £2 (where it was a two-man enterprise), £100 or £1,000. The mode average share capital was £100. The highest share capital was reported at £2,000,100, and the lowest £1. It should be noted that this is not necessarily out of step with companies across the entire register. In 2012-2013 CH reported that 84.6 per cent of companies had a share capital of £100 or less.[395] So, whilst it is plain that a substantial number of the companies in the survey might be described as 'undercapitalised',[396] they are negligibly more or less likely to be so than any other private company on the register.

[395] In previous years, CH have provided a breakdown of the number of corporations by share capital though it appears this has ceased since 2013. The last available information, taken from the register as at 31 March 2013, suggests that in England and Wales 2,188,800 companies had a share capital of up to £100. This represented 84.6% of the total companies on the register. See: CH, *Statistical Tables on Companies Registration Activities 2012-2013* (n 290).

[396] Though, as explored in the penultimate chapter, whether a company is 'undercapitalised' is a tricky business. It is not a straightforward matter of looking at the capital. Though, of course a company with a share capital of £1 might be described as undercapitalised in all conceivable circumstances. See 3.45.

OWNER-MANAGERS

3.47 In a similar vein to undercapitalisation, owner-managed companies are often linked to disqualification. In other words, disqualification targets the small man, rather than the professional executive. Hick's 1998 empirical study of disqualification is largely responsible for this claim,[397] though the author knows of no more recent survey in the area. Not only is Hicks' survey now some two decades old, but its findings were also based on a very small sample size of 33 disqualified individuals who responded to a postal questionnaire. The term 'owner-manager' is one that is rather hard to accurately define; it is largely a case of knowing one when you see one. Some attempt will be made. It is generally understood to be either a company where the directors are also controlling shareholders (either individually or collectively), a 'one man company', or a quasi-partnership.[398] Hicks uncovered in his survey that of those respondents, 28 (84.9 per cent) owned shares in their company; 23 (69.7 per cent) would describe their company as a 'family company'; and out of a smaller sample of 27 directors 14 of those (51.9 per cent) held a controlling interest.[399] This led Hicks to claim that nearly 75 per cent of respondents were owner-managers.[400] Many of the author's suggestions for reform, set out in the penultimate chapter, are hinged upon the assumption that the majority of 'problem' directors are owner-managers of small undercapitalised companies, in line with Hicks' claims. As such, it was deemed necessary to test his findings further, and carry out some up-to-date research. The purpose of doing so was

[397] Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) i.
[398] ibid 8.
[399] ibid.
[400] ibid.

to determine how closely held shares *really* are in the companies of disqualified directors, as based upon the survey data.

3.48 As previously stated, the 285 survey records of disqualified directors were associated with a total of 224 companies. Shareholdings for each company were determined in the same way as the share capital. A search on the CH register was carried out to obtain the last annual return filed. For a number of reasons[401] 16 of companies had to be removed, leaving a total of 208 for the present study. The author went through each annual return and identified the names of the subscribers to the company. This was cross-referenced with the name of the director (or directors) that were disqualified based on the survey data. The following data was recorded for each director:

(a) whether (s)he was also a shareholder of the company;

(b) if so, the amount of that shareholding in percentage terms;

(c) the total number of shareholders;

(d) whether the company was owner-managed;

(e) freehand observations of interest in relation to the company (e.g. 'remainder owned by female relative; likely wife').

In determining ultimately whether the company was owner-managed, the author utilised the definition set out previously. Namely, a company would be considered owner-managed where shareholders who were also directors had either a majority interest in the company or ran it jointly with (often family)[402] others.

[401] Three were companies limited by guarantee; two were LLPs; and for the remaining no records were held.

[402] It was assumed for present purposes that shareholders and directors with the same surname were family members.

3.49 Out of the sample of 208 companies, it was determined that a staggering 90.1 per cent could be described as being owner-managed. Out of the 285 directors, 74.0 per cent were also shareholders of the insolvent company. This figure was slightly lower than expected, but it can be explained by two different reasons. Firstly, some companies in the survey had a sole *corporate* shareholder but when 'backtracking' through CH records for *that* company it transpired that the ultimate owners were one and the same. Therefore, whilst those directors were not recorded as being shareholders of the insolvent company it was still noted as being owner-managed. Secondly, in some cases the directors were not shareholders but were nonetheless part of very closely held (often entirely family) companies of which other (non-disqualified) directors held the controlling interest. Interestingly, 46.2 per cent were what might be described as 'one man' companies. These were companies where there was a sole (disqualified) shareholder-director. 32.7 per cent were '*two* men' companies. Naturally, these were companies with two shareholder-directors; invariably holding shares in 50-50 proportions. Overall, then, one and two men companies made up for nearly 80 per cent of the total survey records.

REFORMING THE PUBLIC REGISTER

3.50 The author took the opportunity to investigate the effectiveness of the DDR on two fronts. Firstly, the content of the DDR and, most importantly, its accuracy.

3.51 *Content of the DDR* It has already been commented upon that the DDR does not contain details as to the underlying factual circumstances leading to a person's disqualification; unlike the IES. This in itself is considered, by the present author, a significant omission that undermines the policy of having an online directory in the first place. A prudent creditor may wish to make searches of the DDR so as to ensure that he or she is not dealing with an unfit person; or a company may wish to make probing enquiries as to the good-standing of a potential appointee to the board.[403] It is accepted that, for the most part, additional details are superfluous; the mere fact that a director is listed should be sufficient to appease the enquiries of all but the most fastidious investigator. However, placing this information on the record, it is argued, would make great strides in the name of the public interest.[404] Having the nature of one's misconduct placed out in the open can be a very powerful deterrent; far more so than just a name on a long list of offenders. It goes without saying that an increased deterrent effect is fundamental to the overall regime, and would go some way to increasing the trust and confidence in it. It is therefore submitted that all records on the DDR *should* contain a misconduct report for public viewing. This would be a well-received extension to the idea of 'naming and shaming', and is something that the IS have got right. CH could learn a lot from this approach.[405]

3.52 As an aside, it is somewhat curious that two separate databases exist in the first place, with different specifications and scope. Perhaps one solution would be to maintain *one* register that is jointly contributed to by both executive agencies, though it is assumed this would require a change in legislation to facilitate.

[403] In a different context, CDDA 1986 checks are often carried out by various professions. For example, the Inns of Court require all barristers before call to certify that they are not disqualified. If checks were carried out (either routinely or randomly), some may slip through the cracks if the register is not properly maintained.
[404] Though as Hicks suggested, awareness amongst the public of the register may be in fact very low: Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 53.
[405] Perhaps somewhat selfishly, the author notes that it would also allow for considerably greater scope for statistical analysis going forward.

3.53 *Accuracy of the DDR* As part of the author's research, some investigations were made to understand the accuracy of the public register of disqualified directors. The reader will recall that CH is required by statute to maintain the DDR. It is comprised of information passed to it by the courts in relation to disqualification orders, and the IS in relation to undertakings. Much has been written in relation to the accuracy and completeness of the DDR in the past. Of particular importance are the two reports published by the NAO; the first in 1993[406] and the later in 1999.[407] In the 1993 report, the NAO found that between December 1991 and November 1992 a substantial 58 per cent of records, out of a sample of over 100 disqualifications, had failed to be published on the register three months later.[408] This report was followed up in 1999. Reflecting in that report on the position in 1993, the NAO noted it was 'disturbed'[409] by the fact that the DDR was 'significantly incomplete'.[410] It was argued by the NAO that the:

> …register has an important part to play in maintaining the standards of company stewardship. The general public and the commercial world are entitled to rely on the accuracy and completeness of the register, the more so because they pay for access to it.[411]

It was suggested within the report that some blame was to be directed at the court system, for failing to notify CH that a disqualification order had been made within a timely fashion.[412] Ultimately, however, the NAO concluded in its 1999 study that since 1993 matters had improved considerably. They reported that there was merely a 'small level of inaccuracy'[413] on the DDR at that time.

[406] NAO Report (n 124).
[407] NAO Follow-Up Report (n 15).
[408] NAO Report, para 4.13.
[409] NAO Follow-Up Report, 57.
[410] ibid.
[411] ibid.
[412] ibid, para 2.42.
[413] ibid, para 2.43.

3.54 The present author was able to conduct his own study on the accuracy and completeness of the DDR in respect of the survey records, in order to give a general appraisal of its state some 15 years following the latest published report addressing the issue. The author wrote a database query to cross-reference between the IES and DDR as obtained on 30th November 2013, to determine whether all of the records in the IES were present in the DDR. In theory, all of the records should have appeared in both databases. However, it transpired that only 112 out of 285 records were recorded on the DDR. In other words, approximately 60.1 per cent of records in the survey were not recorded. In line with the NAO's methodology, the author repeated the process three-months later. The same set of 285 IES records were compared with a new version of the DDR, obtained on 28th February 2014. Cross-referencing revealed that 170 records had been placed on the DDR by that time. To put it another way, 40.4 per cent of records were missing from the public register three months later. It should be noted, as discussed previously in dealing with the methodology of the survey, it was because of these omissions that the author could not cross-verify much of the data between the IES and DDR to check for accuracy.

3.55 It is somewhat self-evident from the figures at hand that there is a large time delay, perhaps caused due to a backlog, between disqualifications being made and reflected upon the DDR. It should also be stated that the blame cannot lay at the feet of the court system in this instance (unlike with the NAO data), as the survey dealt with undertakings; not orders. Based on the survey information, a total of 58 records in the survey were added to the database within three months, which by way of extrapolation suggests it may take up to a further six months before all records are successfully recorded on the DDR.[414]

3.56 This is troubling. To reiterate the NAO's own arguments: there is a great public interest importance in ensuring the accuracy, and therefore the completeness, of the DDR.[415] One primary purpose of the register is to enable the public to know who they are dealing with. This promotes good stewardship of limited companies, as well as acting as a deterrent by ensuring that the wider general public can access the information freely. Any significant delay in the records appearing on the DDR therefore not only harms the underlying purpose of the register, in breach of a statutory obligation, but it also goes some way to defeating the effectiveness of the disqualification regime itself. In turn, this has implications for reducing the trust and confidence placed in it. The time delay may be of particular concern in respect of phoenix companies, where unscrupulous directors often will act as quickly as possible to raise a new company from the ashes, in order to continue trading. If information is not available on the DDR in a timely fashion it could cause issues for potential creditors, who are of course entitled to rely upon the accuracy of the information presented.[416] Whilst there has clearly been improvement since the NAO report in 1993, it is argued here, contrary to their later report, that standards are once again on the decline. This is a matter requiring urgent attention.

---

[414] The author did not carry out any additional tests at routine intervals to see when all records were in fact added; perhaps a missed opportunity.

[415] Moreover, the Cork Committee considered an accurate, publicly, searchable register as being crucial to a successful disqualification regime: Cork Report (n 68) paras 1824-1825.

[416] Despite this, the survey at hand would suggest that phoenixism (with zero reports recorded in the survey period) is becoming less of an issue than it previously was. However, this clearly does not excuse the potential for abuse created by the bad maintenance of the official record.

THE SOLVENCY OF DISQUALIFIED DIRECTORS

3.57 One of the core difficulties, common to all of the mechanisms discussed throughout this thesis, is that of seeking redress against directors who transpire to be impecunious. In terms of disqualification proper, the issue does not arise. However, with the introduction of compensation orders and undertakings, it becomes a major factor for consideration.[417] In short, mechanisms that require a director to account for her misconduct by contributing to the company, or compensate creditors, are only useful where the director in question is worth her salt. Where the individual cannot pay, personal insolvency proceedings will invariably ensue. Section 15B(5) of the CDDA 1986 expressly provides that any compensation order made (or undertaking given) is to be considered a provable debt in bankruptcy, thus it is expected that individuals will be pursued to bankruptcy in appropriate cases. It is worth reiterating that perhaps one unintended consequence will be that more directors will simply submit to personal insolvency proceedings when faced with the threat of compensation.[418] In this section, however, the author will assess how many directors within the survey data were bankrupted within a period of three years from their initial disqualification. Bankruptcy is clear evidence of an inability to pay and, as such, this will enable a more intimate understanding of the demographic of those directors who are likely to be pursued for compensation orders or undertakings. The three-year period was deemed optimal as the SS only has two years from the date of disqualification to proceed against a director for compensation.[419] As such, those found to be bankrupt within that window are, for all

[417] As it is with wrongful and fraudulent trading: 4.18.
[418] 2.47.
[419] CDDA 1986, s 15A(5).

intents and purposes, not worth pursuing. The additional year will allow for some 'spill over' in respect of individuals that the SS might have proceeded against within two years, but in due course, when learning of this subsequent bankruptcy, decide to discontinue. It should be noted that Williams has conducted a similar, more detailed, inquiry into bankruptcy, based upon his own 2008 survey of undertakings.[420] As such, the following analysis is included largely for completeness to enable comparisons to be made between the two data sets, and to bring those findings up to date.

3.58 *Methodology* On 30 November 2016 (i.e. three years following the initial survey), the author wrote a computer programme to automatically match the 285 records in the survey with corresponding entries (if any) in the London *Gazette*.[421] The programme conducted a search based on the name of the director. By cross-referencing common information between the two data sources, it was possible to identify bankrupted directors. Generally, this was done on the basis of a confirmed name and date of birth match. In some cases, it required a match with the name of the company of which the individual directed, or the comparison of a last known address. At least two pieces of matching information were required in order for a record to be included in the survey. However, it transpired that there were no instances where it could not be confirmed, either way, whether the *Gazette* record concerned the individual queried. As such, all 285 records formed part of the final analysis. It is of course possible that a person may have been bankrupted prior to the insolvency of the company that led to their disqualification. As such, only bankruptcies that followed the insolvency of the relevant company were counted in the survey results. The date used in the analysis was

---

[420] Williams, 'Civil Recovery from Delinquent Directors' (n 125).
[421] The *Gazette* is available at <http://bit.ly/1qL6OBf> accessed 26 March 2017

the date that the bankruptcy petition was filed, and not the date that the actual order was made.

3.59 *General findings* Upon analysis, it was determined that 32[422] of the total 285 directors (11.2 per cent) were bankrupted following the corporate insolvency.[423] The small sample size[424] should therefore be considered as a limitation of the analysis to come. A considerable proportion of those (25 records; 78.1 per cent) were bankrupted either before or at around the same time the disqualification undertaking was given.[425] The figures therefore indicate that a disqualified director is most likely to be bankrupted in the interim period between the corporate insolvency and the disqualification. For those remaining directors (7 records), Table 9 below sets out the period of time that had elapsed, following disqualification, before the bankruptcy petition was filed:

Table 9: Number of disqualified directors bankrupted following their disqualification

Period following disqualification (months)	Number declared bankrupt
0-6	1
7-12	2
13-18	2
19-24	0
25-30	1
31-36	1

[422] 11 of those were creditor petitions; 16 debtor petitions. In the remaining 5 cases, the information was not recorded in the *Gazette*.
[423] By way of comparison, Williams found that that 22.4 per cent of directors in his survey were bankrupted. 19.7 per cent were bankrupted within 3 years of the disqualification order being made (which is at the limit of this author's results). See Williams, 'Civil Recovery from Delinquent Directors' (n 125) 325-326.
[424] Again, for comparison Williams' survey yielded 102 bankruptcies out of 456 total records; ibid 326-327.
[425] Williams found that 52.9 per cent were disqualified before or contemporaneously with the disqualification: ibid 326-327.

3.60 Only two directors in the survey fell outside of crucial cut-off period of two-years following the disqualification. In other words, on this survey data, the SS would have had full knowledge of being unable to proceed against 30 out of the 32 bankrupted directors (93.8 per cent) before the statutory time limit expired.[426]

Table 10: Period of disqualification of bankrupted directors

Period following disqualification (years)	**Number declared bankrupt (% of total)**	**Percentage across total sample**	**Difference (%)**
2-5	16 (50.0)	64.2	-14.2
6-10	9 (28.1)	26.3	+1.8
11-15	7 (21.9)	9.5	+12.4

3.61 *Period of disqualification* In terms of the period of disqualification the mean average amongst those bankrupted was significantly higher than across the wider sample, at 6.55 years (median average 5.50 years). As indicated in Table 10 above, based on *Sevenoaks* brackets, it would appear that misconduct considered to be 'minor' (i.e. within the 2-5 years category) is less frequent than when compared to the whole sample. Most of these cases are redistributed, in the case of the bankrupt director, to the highest bracket instead. This has implications for the compensation regime, given that, as stated in the previous chapter, the IS will only pursue the most serious of cases.[427] Again, it is assumed that this is limited to disqualifications made within the middle and top brackets. The reader is reminded that 102 directors (35.8 per cent) across the total

[426] Should the SS have chosen to proceed against the other two, it is likely that the individuals would have been unable to pay going forward in any case. This would lead to 'bad debt' having to be written off by the IS. In recent times, it appears this is becoming more of a problem with 106 claims (accounting for £642,000) having to be abandoned in 2015-16. See: IS, *Annual Report and Accounts 2015-16* (n 249) 99.

[427] 2.42.

sample fell within those brackets. However, 16 of these were ultimately bankrupted (15.7 per cent of those in the top and middle brackets). As such, it is argued that the scope for pursuing disqualified directors for compensation must take that factor into account. In other words, out of the total of 285 directors in the survey the author suggests that only 86 would have made suitable candidates for compensation. This amounts to some 30.2 per cent of the total sample of those disqualified.[428]

3.62 *Allegations* Table 11 below sets out the breakdown of the allegations made against those directors that were bankrupt. Across the 32 directors, there were 58 allegations in total. There is, however, little scope for analysis on this front as the results are not too dissimilar from those seen across the wider survey. One exception relates to a larger incidence of misconduct in dealing with suppliers or customers, which may account for the correspondingly higher average period of disqualification across the demographic.

[428] Incidentally, the average deficit across insolvent companies for those bankrupted was also significantly higher than across the entire sample. Mean deficit: £496,270.74. Median deficit: £212,270.50. Even if the non-bankrupted individuals were pursued, it is questionable how many would be able to afford such sums – many would likely be bankrupted as a result of compensation proceedings, if not the disqualification itself.

Table 11: Number of misconduct allegations in respect of bankrupted directors

Misconduct Description	Allegations	Total (%)
Crown Debt	22	37.9
Accounting	6	10.3
Detriment to creditors other than the Crown	11	19.0
Pre-existing disqualification	1	1.7
In dealing with suppliers and/or customers	5	8.6
Missing Trade Intra Community (MTIC) VAT Fraud	1	1.7
Breach of fiduciary duties	9	15.5
Failing to cooperate with a liquidator	1	1.7
Breach of technical statutory provisions	2	3.4
Total	*58*	*100.0*

3.63 *Conclusion* In summary, it can be said that the number of those bankrupted following disqualification is not overwhelming; but neither is it insubstantial. There are no doubt other factors at play in determining whether a disqualified director should be pursued for compensation aside from those examined here; namely the solvency of the individual and the seriousness of their misconduct. As such, the number of directors actually pursued is likely to be far fewer than the 30 per cent envisaged. The mechanism, therefore, should ultimately be seen as having limited overall utility in the grand scheme of things. In short, compensation orders and undertakings are unlikely to cause any significant shifts in the amount of recovery for unsecured creditors. In light of that, they ought not to be heavily relied on by officeholders or creditors, or held out by politicians, as a magic bullet to remedying the current problems within the enforcement regime. Whilst they will no doubt serve *some* purpose, what has just been described is the true danger: that they are being heralded as something that they are not. Williams puts it in the following terms, which this author adopts in full:

> [the danger is in giving] both office holders and creditors a false sense of security in the ability of the state to improve on outcomes achieved by existing rules. To be sure, there will be some successes, but they may simply come in place of successful recovery by office holders under existing recovery powers [i.e. the private mechanisms].[429]

CONCLUSION

3.64 The author has shown that the vast majority of disqualifications arise from small, owner-managed, undercapitalised, private limited companies. This finding is crucial to the arguments set out in the penultimate chapter, which will deal with measures that might be taken so as to guard against some of the difficulties set out previously. The substantive empirical analysis presented adds yet another dimension of understanding to how disqualification operates in practice. The statistics reveal a great deal about what is working, and what is not. It has been shown that the statutory register is inaccurate and poorly maintained, thereby undermining the objectives of protecting the public, and deterring further directorial misconduct. That aside, it is argued here that undertakings themselves fail, in large part, to embody these underlying aims. Given that undertakings account for some 80 per cent of all disqualifications,[430] this is not a conclusion simply to be brushed under the carpet.

3.65 One primary, inescapable, problem arises from the fact that directors are investigated and prosecuted by a bureaucratic, target-driven, IS. This has, inevitably,

---

[429] Williams, 'Civil Recovery from Delinquent Directors' (n 125) 339.
[430] IS, *Insolvency Service Enforcement Outcomes 2016-17* (n 87).

led to suggestions that the more straightforward cases are being 'cherry picked' as a means of bolstering enforcement statistics. Although the author has not uncovered any evidence supporting that assertion, it is readily apparent that disqualifications arising from misconduct as against the state occupy a considerable portion of the spectrum. As was stated previously in this chapter: Crown debt misconduct is the lifeblood of disqualification. Whilst it might be true that undertakings reduce both the time and cost in dealing with delinquent directors, as compared to court proceedings, this comes as a trade-off for less scrutiny; a potentially target-based enforcement regime; and lower periods of disqualification overall. This is surely out of step with the objectives of the regime. As an inherently flawed system its effectiveness is stunted, and the desirability of maintaining it going forward ought to be challenged.

3.66 An even greater pressing concern of the author is that the recently introduced compensation regime will go much the same way. This must be resisted. It must not simply become a backdoor means of recovering debts owed to the state; masquerading as a mechanism for the protection of the private creditor. To do so would render the effectiveness of the regime nil, when measured against its objectives, and all but destroy public trust and confidence in it. Even if this can be guarded against, the prospects of substantial recovery for the private creditor are slim. It has been demonstrated that a proportionally small number of disqualifications arise from transactions to the detriment of private creditors. Moreover, even where these individuals *are* disqualified it is invariably for a very short period of time. Another problem is, as this chapter has shown, that many disqualified directors suffer bankruptcy following corporate insolvency. As such, the number of potential defendants in compensation proceedings is comparatively small. In short, creditors are unlikely to find that the compensation regime provides anything more than a marginal improvement to their chances of recovery in reality.

3.67 Despite the numerous concerns that commentators, committees, and consultees have expressed in respect of disqualification undertakings, it is quite remarkable that so little has changed over the years. The SBEEA 2015 provided an opportune moment to reorient disqualification towards its primary objective; to protect the public. Whilst it is far too early to examine its impact on the regime as a whole, it is this author's belief that it is unlikely to bring any measurable benefits for private creditors. Yet, simultaneously, it opens up the possibility for abuse and a further deepening of the inherent IS bias towards state-related misconduct. It is business as usual at the IS, and it seems likely to remain that way for the foreseeable future.

Part III

PRIVATE ENFORCEMENT

4

FRAUDULENT AND WRONGFUL TRADING

4.1 The next two chapters of the thesis now turn to deal with the entirely separate matter of private enforcement mechanisms, namely fraudulent and wrongful trading. The first chapter is concerned largely with the substantive law surrounding the mechanisms and will, in the usual fashion, set out the bare essentials of the provisions, followed by an exposition of their objectives. The author will then discuss the effectiveness of the provisions with reference to those objectives. Whilst the improper trading mechanisms are situated within this thesis as having primarily 'private' objectives, the author will also demonstrate that they have potential *in theory* for a 'public' impact through deterrence and directors' disqualification. The author will then explore some of the barriers that are inhibitive of the regime and, in doing so, take a view on effectiveness. Given the linked history between wrongful and fraudulent trading, many of the difficulties faced are common to both provisions. Therefore, first, the general barriers spanning both mechanisms will be considered. The author will then deal with those unique to each of the two mechanisms. Importantly, the impact of the changes made under the SBEEA 2015 in this area also fall to be considered.[431] One

[431] See generally on the changes Edward Taylor and Jack Shepherd, 'Recent developments affecting directors' (2016) 29(3) Insolv Int 42.

particular reform – enabling officeholders to assign, *inter alia*, improper trading actions to third parties – is of such substance that it is dealt with separately in the next chapter.

THE ESSENTIAL PROVISIONS

Fraudulent Trading

4.2 In its current form the fraudulent trading provision under section 213 of the IA 1986 reads as follows:

> (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.

There are therefore three core elements within the section that are required to establish liability:

(a) there must be a carrying on of the business of the company;

(b) it must be carried on with an intention to defraud or for any fraudulent purpose, and;

(c) liability only attaches to those persons knowingly parties to the carrying on of the business.

Wrongful Trading

4.3 By comparison, the wrongful trading provision under section 214 IA 1986 reads insofar as relevant:

> (1) Subject to subsection (3) below, if in the course of the winding up of a company it appears that subsection (2) of this section applies in relation to a person who is or has been a director of the company, the court, on the application of the liquidator, may declare that that person is to be liable to make such contribution (if any) to the company's assets as the court thinks proper.
>
> (2) This subsection applies in relation to a person if—
>
> (a) the company has gone into insolvent liquidation,
>
> (b) at some time before the commencement of the winding up of the company, that person knew or ought to have concluded that there was no reasonable prospect that the company would avoid going into insolvent liquidation or entering insolvent administration, and
>
> (c) that person was a director of the company at that time;
>
> …
>
> (3) The court shall not make a declaration under this section with respect to any person if it is satisfied that after the condition specified in subsection (2)(b) was first satisfied in relation to him that person took every step with a view to minimising the potential loss to the company's creditors as (on the assumption that he had knowledge of the matter mentioned in subsection (2)(b)) he ought to have taken.
>
> (4) For the purposes of subsections (2) and (3), the facts which a director of a company ought to know or ascertain, the conclusions which he ought to reach and the steps which he ought to take are those which would be known or ascertained, or reached or taken, by a reasonably diligent person having both—
>
> (a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the same functions as are carried out by that director in relation to the company, and
>
> (b) the general knowledge, skill and experience that that director has.
>
> …

Similarly, the core elements for liability to attach can be described as follows:[432]

> (a) the company went into liquidation or administration at a time when its assets were insufficient for the payment of its debts and other liabilities and the expenses of the winding up;
>
> (b) at some time before the commencement of the winding up a person who is/was a director knew or ought to have concluded there was no reasonable prospect that the company would avoid going into insolvent liquidation or administration;

[432] As paraphrased from *Brooks v Armstrong* [2015] BCC 561, 665-666.

(c) unless it can be shown, for which the onus[433] is on the director, that she took 'every step' with a view to minimising the potential loss to the company's creditors.

Recent Developments

4.4 The two provisions have remained practically untouched for some three decades. However, two key reforms were implemented as part of the SBEEA 2015. The first relates to administrations. It is noteworthy that both sections 213 and 214 IA 1986 give standing to bring an action only to *liquidators.* However, the substantial rise in administrations led to a call for this to be extended. This was effected, albeit some 30 years following a similar recommendation by the Cork Committee,[434] by section 117 of the SBEEA 2015, which amends the IA 1986 to introduce sections 246ZA-ZC. These sections are identical to section 213 and 214 save that they pertain to administrators and administration. The second reform, dealt with in the next chapter, is that officeholders can now assign, *inter alia,* any wrongful or fraudulent trading action to a third party.

A BRIEF HISTORY

4.5 When the Cork Committee reported in 1982, as with many aspects of insolvency law at the time, it took great issue with the inadequacy of the fraudulent trading provisions as they stood.[435] Originally, the criminal and civil fraudulent trading provisions were twinned within the same section. The Committee noted that, as a result, rules of statutory interpretation demanded that liquidators had to – even in the civil setting – prove their case to the criminal standard. Liquidators, the Committee therefore argued, in civil proceedings, would face 'an unduly stringent burden of proof in relation

[433] ibid.
[434] The Cork Report (n 68) para 1776.
[435] ibid, paras 1758-1760.

to the ingredient of fraud'.[436] As will be shown later in this chapter, it being one of the major hurdles for applicants, proving fraud even to the *civil* standard in insolvency situations is especially difficult; to the criminal standard, immeasurably more so. Cork described the rationale for doing so in the following way:

> We realized that you could never write a law in this country where a jury will convict a man of fraud when all he had done was continue to trade. We had to take it out of the criminal law and make the responsibility a financial one inasmuch as he lost his immunity – limited liability.[437]

A second issue taken up by the Committee was that, given the 'dishonesty' criterion, even the most incompetent, ignorant, or grossly negligent director faced no liability under the fraudulent trading provisions. Moreover, due to the potential for overlap, they noted that a liquidator may be deterred or inhibited from initiating civil proceedings in light of imminent or ongoing criminal proceedings.[438] Thirdly, the Committee took issue with the fact that civil fraudulent trading claims could only be brought in the course of winding up, thereby limiting its applicability, and eliminating all potential for acting pre-emptively so as to mitigate the effects of the fraud on creditors.[439] The combined effects of these highlighted difficulties, in particular the dishonesty requirement, were that the civil provisions were scarcely used in practice.

4.6 The Cork Committee recommended truly radical changes, in particular that the civil fraudulent trading provision *repealed entirely*.[440] In its place, the Committee suggested a new form of civil liability, which they coined 'wrongful trading'. Crucially this would function without requiring proof of fraud or dishonesty, or be subject to the

[436] ibid, para 1759.
[437] Bruce G Carruthers and Terence C Halliday, *Rescuing Business: The Making of Corporate Bankruptcy Law in England and the United States* (OUP 1998) 275.
[438] The Cork Report, para 1759.
[439] ibid, paras 1759 and 1791.
[440] ibid para 1778.

criminal standard.[441] The Committee recommended that the criminal fraudulent trading provision should remain in order to deal with instances of proven fraud.[442] These recommendations were *partly* taken up by Parliament and the civil offence of wrongful trading was duly enacted, in what is today section 214 of the IA 1986. Parliament, however, declined to repeal the civil fraudulent trading provision. Instead, counter to the recommendation, it was merely separated from the criminal provision. The civil provision was re-enacted under section 213 of the IA 1986, with the criminal provisions being moved to section 458 of the CA 1985, now section 993 of the CA 2006. The severance of the two was accompanied by one other substantial modification that Parliament made to the civil element of fraudulent trading under the IA 1986: the applicant. Previously, the provision permitted 'the official receiver, or the liquidator or any creditor or contributory of the company'[443] to bring an action. However, under the reformulation in section 213 of the IA 1986, it became the sole prerogative of the liquidator.[444] Though, as previously adumbrated, the action is now available to administrators.

THE PRIVATE OBJECTIVES

Fraudulent Trading

4.7 The concept of using a company as a vehicle for fraud is no doubt as old as limited liability itself, though fraudulent trading began life as something of an 'experiment'. According to the Greene Committee, who reported in 1926, it was a particular problem of the time that directors who held a floating charge against a

---

[441] ibid, ch 44.
[442] ibid, paras 1777-1780.
[443] Companies Act 1948, s 332(1).
[444] IA 1986, s 213(2).

company of questionable solvency could easily obtain goods on credit so as to 'fill up' their security.[445] The director in question would then appoint a receiver and establish his claim on the floating charge. Reluctant at that time to suggest amendments to the floating charge legislation, the Greene Committee instead made recommendations to implement what became known as the fraudulent trading provisions.[446]

4.8 The *original* rationale for the mechanism is therefore clear. It was to deal with a very specific problem of the time. However, as will have been noted, the provision has evolved somewhat. Because of the original focus as being against those frauds committed solely by directors, only they could be liable under it. This was rectified in the successor provision, namely Companies Act 1948 (CA 1948), section 332, which widened the ambit of liability to encompass 'any persons' found to be knowingly a party to the fraudulent activities. The focus of this thesis is strictly limited to *director* liability, though it should be noted that the nature of fraudulent trading as being applicable to any person is perhaps its most notable feature.[447] Despite the changes over the decades, at its core, the primary objective – when all is said and done – has remained fairly constant. As it was put by Mummery LJ, in the Court of Appeal, in *Morris v Bank of India*:[448]

> [The c]ompensation of those who have suffered loss as a result of the fraudulent trading is the paramount purpose of the provisions imposing civil liability to contribute to the loss suffered.[449]

---

[445] Board of Trade, *Report of the Company Law Amendment Committee* (Cmd 2657, 1926) para 61. This is a practice no longer permitted: IA 1986, s 245.
[446] ibid, para 62. Save minor amendments, their recommendations were enacted in full by virtue of s 75 of the Companies Act 1928, which was later consolidated as s 275 of the Companies Act 1929.
[447] As the case law would later establish, this meant that creditors including, for instance, a third party bank could be held liable under the section: *Morris v Bank of India* [2005] EWCA Civ 693.
[448] ibid.
[449] ibid, [111].

Therefore, in the case of the civil fraudulent trading provision the objective is, rather straightforwardly, to provide a mechanism that permits those who have suffered frauds at the hands of delinquent directors (and by others) to be compensated. The provision provides for this by imposing personal liability upon those found to have traded fraudulently within the terms of the section. The civil mechanism is therefore *not* intended to punish the errant director though, as one might expect, it was recognised that such persons were no doubt deserving of punishment in some cases. Thus, the *criminal* provision fills the particular lacuna where the conduct is deemed so severe as to warrant prosecution in the public interest. It should be noted that, in line with the scope of the thesis, the primary focus of this chapter is on the civil fraudulent trading provisions. With that said, however, much of the discourse will equally apply to criminal proceedings and they will be referred to where necessary throughout.

Wrongful Trading

4.9 Given that wrongful trading was a child of Cork, that provides a suitable starting point for determining the rationale for and objectives of the mechanism. It has already been expressed that wrongful trading was designed to overcome the perceived difficulties of fraudulent trading. As the Committee set out in its Report under a heading 'the justification for the new concept':

> A balance has to be struck. No one wishes to discourage the inception and growth of businesses, although both are unavoidably attended by risk to creditors. Equally a climate should exist in which downright irresponsibility is discouraged and *in which those who abuse the privilege of limited liability can be made personally liable for the consequences of their conduct*. We believe that our proposals…strike a fair balance between those two conflicting needs. We regard them as of the greatest importance, and their implementation as a matter of urgent necessity.[450]

[450] The Cork Report (n 68) para 1805 (emphasis added).

The rationale is therefore clear in that, as expressed in the first chapter, the mechanisms discussed in this thesis are all ultimately designed to retain a sensible balance between access to limited liability to encourage entrepreneurship on the one hand, but to prevent its abuse on the other. However, the primary objective of the provision is more difficult to pin down. One purpose of the mechanism was set out by Vinelott J in *Re Purpoint Ltd*[451] as being to 'recoup the loss to the company so as to benefit the creditors as a whole'.[452] Moreover, in a command paper published by the DTI in response to the Cork Report it noted that one objective would be to:

> [L]ead to a material improvement in the position of unsecured creditors by curbing the activities of irresponsible directors and by ensuring that companies act more swiftly when faced by the prospect of insolvency.[453]

In other words, by ensuring prompt action amongst directors in the face of insolvency, the instances of misconduct amounting to wrongful trading would be reduced, thereby improving the overall position for unsecured creditors. *Prima facie* it can certainly be argued that wrongful trading embodies as its primary objective a compensatory function similar to that found in fraudulent trading. But, in fact, the true position appears to be that through encouraging higher directorial standards the hope of the DTI at that time was that the mechanism would simply never have to be utilised. Williams and McGee have indeed cited this as being the most important objective of wrongful trading.[454] In a similar vein to fraudulent trading, wrongful trading is therefore not designed to be a

[451] [1991] BCLC 491.
[452] ibid, 499.
[453] DTI, *A Revised Framework for Insolvency Law* (Whitepaper, Cmnd 9175, 1984) para 27.
[454] Interestingly, Williams and McGee in their study concluded that the wrongful trading was ineffective as it did not fulfil the objectives of the Cork Committee. Yet, in truth it cannot be said that encouraging higher standards, as they submit, was really Cork's priority: Christina Williams and Andrew McGee, *A Company Director's Liability for Wrongful Trading* (ACCA Research Report 30, 1992) 25.

penal mechanism.[455] This approach is therefore in some ways at odds with original intention of the Cork Committee, who clearly envisaged that wrongful trading would – first and foremost – be about compensating creditors.

THE PUBLIC OBJECTIVES

4.10 Keay has argued that fraudulent and wrongful trading serve both a public *and* private function.[456] As alluded to in Chapter 1, in some instances the dividing between strictly 'public' or 'private' enforcement mechanisms is blurred.[457] This is particularly true in the case of wrongful trading given what has just been stated about its primary objective. The private functions relate to their ability to compensate creditors. The public functions lay in the improvement of standards of management generally; providing a deterrence from wrongdoing; and the interaction with disqualification.[458] It is this author's perspective, to the contrary, that although they may be said to serve certain public functions in *theory*, the practice is somewhat different.

Deterrence and Raising Standards

4.11 Deterrence has already been dealt with in significant detail previously in this thesis.[459] The author does not intend to repeat those points, though it should be noted that many of those made – particularly in respect of awareness – apply equally in this context. The concern of this author is accurately summarised by Ball:

---

[455] *Re Produce Marketing Consortium Ltd* (1989) 5 BCC 569.
[456] Andrew Keay, *Company Directors' Responsibilities to Creditors* (Routledge-Cavendish 2007) 67
[457] 1.10.
[458] Keay, *Company Directors' Responsibilities to Creditors* (n 456) 67-68.
[459] 2.11.

> 'The deterrent effect of law obviously depends upon…the knowledge of the law and the punishment prescribed…*A law can have no deterrent influence upon a potential criminal if he is unaware of its existence*'.[460]

Thus, a person unaware of the existence of proceedings that may be taken against them is wholly unlikely to be deterred from such a course of conduct. As discussed previously, the state takes limited steps to bring matters such improper trading, and the associated penalties, to the attention of directors.[461] Coupled with the exceedingly low volume of cases, a matter dealt with below, it seems unlikely that awareness is high. The author makes the point that if awareness of by far the most widely used mechanism – disqualification – is low, then the mechanisms discussed in this chapter immensely more so. Consequently, it is suggested that any deterrent effect is commensurately low. This is especially troubling in cases of fraud, as the consequences of such wrongdoing can be especially damaging to creditors and wider society.[462] A successful regime, therefore, should embody a strong deterrence agenda, and it is somewhat obvious to this author a lack of awareness has dogged current efforts in this regard. But, in turn, this has a knock-on effect in terms of improving standards. Again, this was dealt with substantively in relation to disqualification. In short, it cannot be said that standards of directorial behaviour will be improved if those subject to the regulation are not aware of what conduct it seeks to control. The state cannot expect this knowledge to be obtained by directors through osmosis; proactive steps are needed. In the case of wrongful trading this omission is especially noteworthy given its primary aim of raising

---

460 John Ball, 'The deterrence concept in criminology and law'(1955) 46(3) J Crim LC & PS 346, 347-348 as quoted in Kirk Williams, 'Public knowledge of statutory penalties: the extent and basis of accurate perception' (1980) 23(1) The Pacific Sociological Review 105, 109 (emphasis added).

461 2.17-2.20.

462 See National Fraud Authority, 'Annual Fraud Indicator 2013' (June 2013) <http://bit.ly/1zU4oQI> accessed 01 January 2016; R3, 'The Fraud Landscape: Insolvency and the fight against fraud' (January 2015) <http://bit.ly/17dWJ7L> accessed 01 January 2016.

standards thereby obviating the need for its use. Thus, the author is forced to conclude that wrongful trading fails to achieve its primary objective as a result of the state's almost total failure in this regard. The obvious solution to this, as will be dealt with in the penultimate chapter, is to raise awareness through education and training.

Directors' Disqualification

4.12 The even stronger point made here however, manifested on official data, relates to directors' disqualification. Another form of disqualification not yet discussed arises from CDDA 1986, section 10. It provides that where the court makes a declaration that a person is liable to make a contribution to the company's assets for wrongful or fraudulent trading, it may also make a disqualification order for a period not exceeding 15 years. It is contended that Keay's comment that disqualification provides a public enforcement element within the context of improper trading is confined merely to academic theory. It benefits from limited practical observation. Whilst it is the opinion of this author that it *should* occupy a far more prominent position in the disqualification arena, the evidence examined below is conclusive of the fact that it simply does not.

4.13 A spate of FOIA 2000 requests by this author to CH and IS conclusively illustrates that even for those few individuals found liable for improper trading, the numbers disqualified are infinitesimally small. Table 12 below identifies the number of disqualifications made under CDDA 1986, section 10, since its inception:

Table 12: Disqualification Orders notified to the Secretary of State pursuant to section 10 CDDA 1986: 1986-2015

Year *Indicates grouped	Number of Disqualification Orders
1986-1990*	0
1990-1991	10
1991-1992	1
1992-1993	9
1993-1994	2
1994-1995	1
1995-1996	1
1996-1998*	0
1998-1999	2
1999-2000	1
2000-2015*	0

4.14 According to the official data, the total number of disqualifications made under section 10 is 27, all occurring within the years 1990-2000. Since that time there have been no further disqualifications made under that section to date. What is particularly interesting is that the surge of section 10 disqualifications in the 1990's dissipated around the same time as the implementation of the IA 2000, which introduced disqualification undertakings. Although not necessarily causative, it seems likely that since this time, what with the vast majority of disqualifications occurring via undertakings, section 10 *orders* have been all but forgotten. However, on this point it may be deduced from statistics provided by the IS that even if this is the case, and it is their practice to pursue such individuals for undertakings, the numbers are equally small. The official statistics for 2016-17 suggest, for example, that there was only *one* allegation of 'insolvent trading' out of a total of 1272.[463] No defined category in the

[463] IS, *Insolvency Service Enforcement Outcomes 2016-17* (n 87) Table 1C.

statistics relates to fraudulent trading and therefore it is deduced that any they would fall into the 'Other' category. For 2016-17 there were zero such allegations that fell into that category.[464]

4.15 Given that there is not even a need for an application by the officeholder for disqualifications to be made under section 10, as the court may make an order of its own volition, it would appear that its lacklustre usage falls squarely in the hands of the judiciary. Particularly in the case of fraud it is argued here that, where proven, disqualifications should in fact routinely be ordered. In this author's mind, there can be no greater display of misconduct than fraud so as to warrant being barred from directorial practice. It seems at odds with the objectives of *disqualification* to swiftly and forcefully pursue those that commit relatively minor wrongdoing, for instance a failure to pay modest Crown debts.[465] Yet, when the court is physically faced with an individual proven to have committed acts so grievous to the extent of being labelled as 'dishonest' it appears that such a person will in effect never be barred. Indeed, this is *contrary* to the very idea of a deterrence. One possible solution, of course, is to implement some mechanism of automatic disqualification, as in Australia.[466] This has been proposed by various commentators, including the Cork Committee,[467] though to more general effect, and the concept has largely been shunned by Parliament. What is suggested here, however, is the potential for the legislation to provide – namely in cases of fraudulent trading – for a presumption that the individual found liable should be

---

[464] ibid.
[465] 3.20.
[466] Corporations Act 2001, s 206B (Australia). See generally Stephen Griffin, 'Accelerating disqualification under section 10 of the Company directors disqualification act 1986' 2002 2(Mar) IL&P 32.
[467] Insolvency Law and Practice: Report of the Review Committee (Cmnd 8558, 1982) para 1817

disqualified, except in cases where information prevailing at the time would prevent such an order. The more heinous the fraudulent trading, the more difficult it should be to rebut the presumption that there should be an order for disqualification.

4.16 The author has therefore demonstrated that disqualification in all of its history has hardly ever been used as a mechanism of enforcement subsequent to a finding that an individual has engaged in improper trading. It is for this reason that it is concluded that the 'public' utility of either mechanism is muted. In terms of the effectiveness of the regime, this is from one angle highly damaging, and from another simply a missed opportunity.

THE NUMBER OF IMPROPER TRADING CASES

4.17 One of the most cited criticisms of the improper trading mechanisms is that there is a paucity of actions brought and, what is generally drawn from that, is they are ineffective.[468] In modern discourse, the majority of the attention in this regard is focused on wrongful trading. It was known as long ago as the Cork Report, and even before then, that the number of fraudulent trading cases brought was infinitesimal.[469] In fact, it was that, amongst other factors, which led to calls by the Cork Committee for the abolition of the civil fraudulent trading mechanism. To put it bluntly, commentators seem to now be bored of repeating those same arguments and, in numbers terms, fraudulent trading is treated as being 'virtually dormant'.[470] There was originally,

[468] For instance: Adrian Walters, 'Enforcing Wrongful Trading – Substantive Problems and Practical Disincentives' in Barry Rider (ed), *The Corporate Dimension* (Jordans Publishing 1998); Fidelis Oditah, 'Wrongful trading' [1990] LMCLQ 205; Bree Taylor, 'Wrongful trading' Recovery (R3, Spring 2015) 16.
[469] The Cork Report (n 68) para 1776.
[470] Ian Fletcher, *The Law of Insolvency* (4th edn, Sweet & Maxwell 2009) 27-024.

however, a significant hope that wrongful trading would be the solution. Indeed, there is still optimism expressed in the literature that the *potential* of the mechanism is very great indeed.[471] It must be remembered that the whole 'point' of wrongful trading, on the view of the Cork Committee, was to overcome many of the historic difficulties associated with fraudulent trading, thus increasing the number of actions taken against delinquent directors, and ultimately improving returns for creditors. And, the reader will be reminded, that the Committee viewed this as being a matter of the 'greatest importance' and of 'urgent necessity' to resolve. Given the primary objective of the mechanism, it might be said that the true sign of an effective wrongful trading regime is *no sign of it at all*. Though, causally this can only be accurate where absence is caused by an improvement in standards which, as the author has set out, there is no evidence to suggest has been the case. To take the Cork approach, another view of determining effectiveness might be to look at the number of cases, and to determine whether things have improved since that time. Yet, analysis by Williams, up to 30 September 2013, showed a mere 16 reported decisions on substantive liability under the section since 1986. In 11 instances the liquidator was successful, and therefore no success was found in five of those cases; 13 cases dealt solely with procedural matters arising from section 214 (but not substantive liability). Therefore, there were a total of 29 reported applications under section 214 at that time.[472] For completeness, the author carried out – utilising the same methodology as Williams – a search for recent cases up to the time of writing. There have been an additional four reported wrongful trading cases since

---

[471] Richard Williams, 'What Can We Expect to Gain from Reforming the Insolvent Trading Remedy?' (2015) 78(1) MLR 55, 56
[472] ibid, 60-61.

that time, one of which was Scottish.[473] One case dealt solely with procedural matters arising from section 214.[474] In the three remaining substantive decisions,[475] the liquidator only found favour in one.[476] Thus, to date there have been 33 reported applications. These are small numbers indeed. The expected revolution has therefore surely been a failure in numerical terms. It is hoped by some that the SBEEA 2015 reforms, in particular that of assignment, might invigorate the usage of the mechanism. The reader will be spared from that discussion until the next chapter. But, it is suggested here that the expectation of a larger number of cases is based upon a false premise, i.e. that 'the current modest levels of litigation…are [not] dramatically out of line with instances of insolvent trading'.[477] That is also the argument recently set out by Williams, who notes that there is no evidence, empirical or otherwise, presented in the Cork Report or the wider literature that suggests otherwise. In short, wrongful trading as a form of misconduct may simply not be as common as was anticipated. Yet this author goes further, and argues that there is nothing in the Cork Report itself which even *suggests* that wrongful trading was ever a widely experienced problem. Whilst it is true that there is a demand for 'urgent' action in this regard, it was the *assumption* of subsequent commentators that the need for urgency was driven as a result of there being a widespread problem. This author was fortunate to have had access to the private papers of Muir Hunter QC, who kept detailed records of his time sitting on the Cork

[473] *Paton v Martin* [2016] SC AIR 57.
[474] *Brooks v Armstrong [2016] EWHC 2893 (Ch);*
[475] The other two being *Re Ralls Builders Limited* [2016] EWHC 243 (Ch); *Brooks v Armstrong* [2015] BCC 561.
[476] The Scottish case.
[477] Williams, 'What Can We Expect to Gain from Reforming the Insolvent Trading Remedy?' (n 471) 77.

Committee.[478] On the author's reading of the materials instead the reality appears to be that there was considerable ill-feeling towards directors that traded wrongfully, but were not dishonest, and 'got away with it'. Cork in particular appeared to view it as something of a personal mission to fill what he viewed as being a lacuna in the law as it stood at that time. In fact, Cork seemed adamant that delinquent directors of this ilk should be made *bankrupt*, and wrongful trading apparently seemed to be present a sensible option of achieving that. It was therefore this lacuna – rather than there being any great numerical concern – that led to the call for urgent reform, and was thus the driving force behind the wrongful trading rule. This is also borne out impliedly in the work of Carruthers and Halliday, who conducted a series of personal interviews with Cork on the subject.[479] And thus, there still remains to this day a dearth of evidence which might suggest that the type of conduct the mechanism was intended to counteract was, or indeed, *is,* a particular problem. It is therefore submitted, alongside Williams, that the reality is that wrongful trading probably does not exist in the wild with any notable frequency. As previously noted, this finding is consistent with the disqualification statistics.

GENERAL BARRIERS TO CLAIMS

Director Impecuniosity

4.18 The issue of director impecuniosity has been discussed at significant length previously.[480] But, indeed, the impecuniosity of potential defendants is a difficulty common to all of the enforcement mechanisms discussed in this thesis. In the case of

[478] And for this opportunity I must express my sincere thanks to Dr John Tribe.
[479] Carruthers and Haliday (n 437).
[480] 3.57.

improper trading, it will undoubtedly be at the forefront of the officeholder's mind. Put simply, it would defy logic to pursue a director who is not worth her salt. It will be remembered that this author has suggested that Cork's intention for the wrongful trading mechanism was to bankrupt delinquent directors. But, in truth, if directors are *already* on the verge of their own insolvency before they are required to make a contribution, any resultant success is purely symbolic. Again, this is a problem particularly noticeable in the case of owner-managers, many of whom will inject their own personal assets in to their company in order to try and save it when insolvency nears. Others will be subject to personal guarantees and therefore the insolvency of the company may lead to their own demise in short order. Although this issue arises independently of the mechanisms themselves, it is argued that it must be a factor for consideration in determining their effectiveness. This is because it presents a strong disincentive for an officeholder to commence proceedings, even in circumstances where the case is otherwise evidentially strong. The net result, of course, is that creditors lose out.

Standing

4.19 One concern that has been revisited in the commentary over the years has been the limited scope of the *locus standi* of the improper trading provisions. This has particularly been true of fraudulent trading, mainly due to the fact that it saw a reduction in its scope post-IA 1986 as explored previously. It is argued here that the restrictive approach taken to standing has been inhibitive of the regime over the decades. At the very least, there are compelling arguments to favour the widening of the provision to permit *creditors* to bring improper trading actions. With that said, the author's argument falls by the wayside to some extent following the reforms of the SBEEA 2015. The assignment provision in effect permits a circumvention of the *locus standi* requirements and can, in theory, permit a creditor to take action; albeit only following officeholder approval. Nonetheless, the author will put his case as it is yet too soon to know whether officeholders will permit creditor actions in practice. And, that is to say nothing of the past three decades of wasted opportunities for creditors.

4.20 An examination of Hansard reveals an insight into the reasoning as to why the government of the day sought to narrow the standing requirements in relation to fraudulent trading. By extrapolation it can be assumed that similar logic applied to setting the standing requirements for wrongful trading at the point of inception. Parliamentary Under-Secretary of State for DTI, Mr Alexander Fletcher, explained that:

> … [fraudulent trading] proceedings should be available only to the liquidator and…therefore any imposition of personal liability on directors and others should benefit creditors as a whole…Creditors will no longer be able to institute proceedings for their own individual benefit.[481]

The reason for the shift, it therefore might be inferred, relates to the fact that an individual creditor could pursue a fraudulent trading claim for her own benefit, potentially to the detriment of others. In line with this stance, Keay has argued that the position under section 213 is therefore more equitable than under any of its predecessors.[482] This is because the older provisions may have consequently had the effect of placing the respondent in an impecunious state following a single successful creditor claim, thereby inhibiting her ability to pay other creditors who have failed to initiate proceedings, or were simply slow in doing so.[483] In other words, Keay envisaged an inequity in the potential for a 'race to the courthouse' scenario amongst creditors. It should be noted that there is little evidence to suggest that this actually occurred in

[481] Fletcher A, HC Deb, 05 June 1985, vol 80, c178W.
[482] Keay, *Company Directors' Responsibilities to Creditors* (n 456) 33.
[483] ibid.

practice. In contrast, however, any award made under the current provisions is specifically a general contribution to the assets of the company, for the benefit of unsecured creditors,[484] and not the individual applicant. This stands to reinforce the *pari passu* principle. A second, but related, issue that stems from this is what Milman has described as the 'spirit of collectivism'.[485] In other words, it may, purely on policy grounds, be undesirable to promote or allow any action which militates against a *pari passu* type distribution. This author's suggestion of widening the provisions, therefore, might be considered by those such as Keay and Milman to fly in the face of collectivism ideology and, as a result, be undesirable in policy terms. However, there are many diverse reasons as to why an action may be justifiable in spite of policy concerns, three of which are described here:[486]

> (a) not least that it may indeed be equitable that a creditor who successfully brings proceedings at his own expense should have the full benefit of any damages award as in any area of the common law. Any dividend stemming from the assets pot following winding up would be deducted from the award, in accordance with general principles,[487] so as to prevent issues of double recovery;
>
> (b) a creditor might instigate proceedings as trustee of himself and a particular class of creditors by previous arrangement so that, in effect, any costs, as well as any gains, are shared amongst this class;
>
> (c) in some circumstances, there may be certain creditors who are aware of the company's insolvency but continue to trade at the risk of default, whereas other creditors may be deceived as to the creditworthiness of the company.

In terms of effectiveness, the author's position is straightforward. In limiting the *locus standi*, although its impact is not measurable, pre-2015 creditors have been

[484] *Re Oasis Merchandising Services Ltd* [1995] BCC 911

[485] On the issue of the tort of deceit as an alternative action in the fraudulent trading context David Milman, 'Two cases of interest for company directors operating in the twilight zone' (2008) 21(2) Insolv Int 25, 27.

[486] Similar justifications were raised by Lord Denning: HL Deb 01 April 1985, vol 462, col 40.

[487] As in *Komerçni Banka AS v Stone & Rolls Ltd* [2003] 1 Lloyd's Rep 383 for example, a case in the tort of deceit.

unreasonably prohibited from commencing proceedings in otherwise actionable cases. Thus, in circumstances where the officeholder herself is reluctant or unable to commence proceedings even pecunious creditors that are willing to take matters into their own hands are left with no alternative, without any real justification. Hopefully, following the SBEEA 2015, this position will change as assignment takes hold.

BARRIERS TO WRONGFUL TRADING CLAIMS

The 'Net Deficiency' Requirement

4.21 One of the most perplexing difficulties with the wrongful trading provision relates not to the establishment of liability, but the way in which compensation is calculated should the officeholder succeed in her action and, as a corollary, the circumstances in which a court will exercise the discretion to make a contribution order. One particular issue in this regard, which the author refers to as the 'net deficiency requirement', has reared its head fairly recently to considerable criticism by Gabriel Moss QC.[488] In fact, the current approach has been described by that esteemed commentator as both 'a disgrace to our jurisprudence'[489] and 'unjust and absurd'.[490] In *Re Ralls Builders Limited*[491] and *Re Ralls Buildings Limited (No. 2)*[492] it was held by Snowden J that the directors in question had traded wrongfully, contrary to section 214 IA 1986. However, even in the absence of the directors being able to establish the 'every step' defence, the learned judge declined to make a contribution order. Thus, the unsecured creditors of the company got nothing for the efforts of the liquidator. In fact,

---

[488] Gabriel Moss, 'No compensation for wrongful trading – where did it all go wrong?' (2017) 30(4) Insolv Int 49.
[489] ibid 53.
[490] ibid 51.
[491] [2016] EWHC 243 (Ch).
[492] [2016] EWHC 1812 (Ch).

as Rajak notes, they 'suffered substantially through the depletion of assets incurred by long and expensive litigation'.[493] Snowden J took this approach because, in short, although new liabilities had been incurred during the period of wrongful trading, existing creditors (primarily the bank) had been paid to a similar extent to the effect that there was no material increase in the net deficiency of the company. Or, if there was an increase in the deficiency, there was no satisfactory evidence, on the balance of probabilities, that it was caused by the directors. This was not a position adopted on a whim. Indeed, Snowden J's view was in line with a number of existing decisions. Following a detailed examination, the learned judge went on to confirm the approach of Vinelott J *Re Purpoint*[494] and Park J in *Re Continental Assurance*,[495] holding that:

> [T]he fact that any contribution to be made under section 214(1) must be distributed *pari passu* among the general body of unsecured creditors of the company is a significant pointer to the fact that the purpose of section 214 is not to provide differential redress for individual creditors, depending upon an assessment of the extent of their loss caused by the period of wrongful trading. So, for example, a creditor whose debt was incurred after the relevant date cannot claim to recover 100% of his loss in priority to a creditor whose debt was incurred prior to that date and who may only have been marginally disadvantaged (or not disadvantaged at all) by the continuation of trading.[496]

Although, as noted by Moss, the authorities relied upon were without exception first instance decisions and thus Snowden J could have adopted a different course if he had seen fit. To the contrary, it was made clear by the judge that any change to what he himself described as being a 'shortcoming'[497] of section 214 must now nonetheless be for Parliament.[498] He described the root problem with the net deficiency requirement in the following way:

---

[493] Harry Rajak, 'The complex story of wrongful trading' (2017) 392 Co LN 1, 4.
[494] [1991] BCLC 491.
[495] [2001] BPIR 733.
[496] *Re Ralls Builders Limited* [2016] EWHC 243 (Ch), [236].
[497] ibid, [279].
[498] ibid.

> The real sin of the Directors, so far as the unsecured left in the liquidation are concerned, is the manner in which the continued trading facilitated the repayment of the Bank and some existing creditors whilst leaving new creditors unpaid[499]

Therefore, whilst apparently sympathetic to those 'new' creditors that had suffered at the expense of existing creditors, he felt unable to make the contribution order sought by the liquidator on the basis of existing precedent. In the slightly later case of *Brooks v Armstrong*[500] David Foxton QC sitting as a Deputy Judge of the High Court followed the same approach of his brethren, thus apparently confirming that this is the position to be adopted for the future, save for intervention from either Parliament or the Court of Appeal. It goes without saying that, at present, there is no Parliamentary will to attend to the matter. Similarly, the likelihood of a case reaching the Court of Appeal is slim, as the officeholder has to weigh up the serious risk that he may simply be throwing good money after bad.

4.22 Moss sets out what is, in his view, the absurdity of the current legal position with a simple yet stark illustration.[501] Imagine a director, who during a period of insolvent trading takes on £1 million worth of new liabilities that the company had no reasonable prospect of paying. Should the director cause the company to pay off £1 million of old liabilities in the same period, then no contribution order could be made on the current approach in *Re Ralls Builders Ltd* due to the net deficiency being zero. Moss therefore concludes that this 'provides directors with the perverse incentive of continuing to trade as long as they are careful to "rob Peter to Pay Paul" and to make sure that the net deficit remains constant'.[502] Moss describes the original intention of the

[499] ibid.
[500] [2016] EWHC 2893 (Ch).
[501] Moss (n 488) 51.
[502] ibid.

Cork Committee as being that directors should have to compensate creditors where they took on liabilities without any real prospect of being able to pay them.[503] Thus, if this formulation were adopted the director in the above example would be liable for the sum of £1 million; namely the liability incurred during the period of insolvent trading, rather than the company's net deficiency. He therefore suggests, given Parliament expressed no contrary view to the nature of the mechanism as proposed by the Committee, that it is that view that they silently adopted. Thus, he argues, the present position arises from statutory misinterpretation, originating from the early decision of Knox J in *Re Produce Marketing Consortium Ltd*.[504] The author has considerable sympathy with Moss' pro-creditor argument. However, there are two points where the analysis falls down. As has been recognised by a number of commentators, including Sealy and Milman, Parliament ultimately did not see fit to accept the recommendations of the Cork Committee in full in this context. Therefore, whilst the bald concept was adopted, it cannot be assumed – as Moss appears to – in view of the DTI's silence on the matter that the spirit of the provision was adopted in full. Moss' argument is therefore based upon a false premise. In fact, it is suggested here that part of the reason for this lack of detail was, as recognised by Knox J in *Re Produce Marketing Consortium Ltd* that Parliament purposefully chose to afford the courts a large amount of discretion in the exercise of the remedy and its development. It should also be recalled that Parliament did not see fit to intervene at the most opportune moment and correct the position when passing the SBEEA 2015. It therefore seems the current approach to this issue is here to stay. There is however a further insuperable difficulty with Moss' argument which,

[503] ibid, 50.
[504] (1989) 5 BCC 569.

upon reflection, confirms in this author's mind that the current course adopted in the recent cases must be the correct one. To adopt the approach of the Cork Committee, and therefore Moss, it is argued, would orientate the mechanism as being one that is *penal* and not compensatory. There is little doubt that Cork himself very much intended the provision to have a penal effect; though without it expressly being penal on the face of the provision. However, that is not the approach that Parliament ultimately adopted. Thus, as with disqualification, any construction of the section that might exhibit punitive intentions must be resisted. Or, if the punishment of directors in this context is deemed to be desirable, then the law must be changed to reflect the change in appetite.

4.23 Practically, this creates evidential difficulties for the officeholder who must prove both a net deficiency *and* a causal link between that deficiency and the director's conduct. This is no doubt a time consuming and costly process in itself. But, as is now made obvious from the recent authorities, doing this properly is crucial to success or failure. In terms of the bearing of the current position upon the effectiveness of the wrongful trading regime, notwithstanding the arguments made previously, it cannot be denied that it paints a very stark picture indeed for creditors. If an aim of wrongful trading is to compensate creditors who have suffered at the hands of delinquent directors, then the recent case law in this area can be described as nothing other than a significant blow to that endeavour, even if it is done for the proper reasons. In terms of the other objectives of wrongful trading, namely deterrence and the raising of standards amongst directors generally, again, the current position is a considerable inhibitor; yet again confirming the significant difficulties that an officeholder will have in pursuing delinquent directors even where there is a *prima facie* strong case of misconduct. In fact, the author suggests that the current approach may even *encourage* reckless trading. If *very* careful, a director could in theory continue to trade whilst insolvent – incurring additional liabilities knowing they are unable to be repaid in the process – *in perpetuity* without wrongful trading liability so long as the net deficiency remains at, or close to, zero, and so long as comprehensive accounting records are kept to evidence the same.

BARRIERS TO FRAUDULENT TRADING CLAIMS

The Dishonesty Requirement

4.24 The need for proof of *dishonesty* for liability to attach under section 213 is nowhere to be found in the wording of the section itself. Yet it is recognised, even in the civil context, as being necessary to satisfy either of the 'intent to defraud' or 'fraudulent purpose' ingredients.[505] It is argued here that the miniscule number of fraudulent trading cases brought is primarily a result of officeholder reluctance stemming from the existence of this dishonesty requirement. In fact, there is little doubt in the mind of this author that it is the primary barrier to a successful fraudulent trading action.[506] This may well be appropriate. Fraud is a very serious allegation and it is therefore quite right that it is proven to a high standard in order for liability to attach, in the interests of justice. The point made by the present author here is that, in fact, the need for the requirement is entirely erroneous and it has arisen primarily as a result of a misconstruction of the section in two early decisions of Maugham J.[507] That notwithstanding, the courts have in any case introduced significant confusion and

[505] *Scott v Commissioner of Police of the Metropolis* [1974] 3 WLR 741, 819.
[506] Keay, *Company Directors' Responsibilities to Creditors* (n 456) 51.
[507] *Re Patrick and Lyon Ltd* [1933] Ch 786; *Re William C Leitch Brothers Ltd* [1932] 2 Ch 71.

adopted a patchwork approach to the dishonesty requirement.[508] It is submitted that the failures in this regard have in reality been what has led to the slow, and painful, death of the mechanism. It seems likely to the present author that it was the original twinning of the civil and criminal fraudulent trading provisions, and its penal interpretation, that gave rise to this approach. Yet, the dishonesty requirement has in this author's view rendered the effectiveness of the mechanism close to nil. This is because proving dishonesty is extremely difficult even in 'ordinary' circumstances. Doing so in insolvency situations where it has to be very carefully distinguished from mere ineptitude or poor commercial judgment, borders on the impossible. It will be advanced that *knowledge*, it being a far more morally neutral concept, ought to be the appropriate measure in this context. Knowledge is also far more straightforward to ascertain in the context of commercial decision making. On this point, albeit in the broader civil context, Davies has written that:

> [D]ishonesty is a distraction from the essence of the inquiry into the defendant's knowledge. After all, a defendant will not be liable unless he or she fulfils the necessary criteria of knowledge a defendant who genuinely and legitimately knows nothing regarding the primary wrong will not be considered to be dishonest.[509]

As will be addressed below, it is also contended a test based on knowledge must have been the pure intention of the legislator – an intention set adrift following the decisions of Maugham J, and one never steered back on to a correct heading.

4.25 *Judicial reluctance* However, this is not merely a question of semantics. Not only is it true that substantial judicial energy has been expended on dealing with abstract

---

[508] Birks has referred to 'judges cast adrift on the sea of an undefined and objective dishonesty' in Peter Birks, 'Accessory Liability' [1996] LMCLQ 1, 6; Lord Millett dissenting in *Twinsectra Ltd v Yardley* [2002] UKHL 12 similarly noted at [134] that 'the introduction of dishonesty is an unnecessary distraction, and conducive to error'.

[509] Paul Davies, *Accessory Liability* (Hart 2015) 121.

concepts such as dishonesty, but there is evidence to suggest that in the context of insolvent companies, judges are simply reluctant to 'brand' an individual as dishonest in situations of commercial decision making, thus further diminishing the effectiveness of the mechanism.[510] Lord Hutton in *Twinsectra Ltd v Yardley*[511] insinuates as much in his judgment when he said that a 'finding by a judge that a defendant has been dishonest is a grave finding, and it is particularly grave against a professional man'.[512] Some might question *why* it is 'particularly grave' as against a professional. It seems uncontroversial to this author that it must be inappropriate, even in cases involving professionals, that judges should shy away from branding an individual dishonest where he has fallen below the required standard. Indeed, such reluctance has been criticised by Peter Smith J, who has stated it to be erroneous:

> First there is no justification in applying a stricter principle against a Defendant merely because he is a professional. It is no less grave for a non professional to be accused of dishonesty. The courts have always been reluctant wrongly in my view to adopt that stance. Second, cases in the last decade have shown sadly that there are plenty of professional men who act dishonestly.[513]

In terms of the effectiveness of fraudulent trading uncertainty for the liquidator is compounded by judicial reluctance, thus reducing the desirability of mounting an action.

4.26 *The appropriate test* But, even if one accepts the legitimacy of dishonesty within fraudulent trading, the discourse as to what *standard* of dishonesty is required has itself had a rather chequered history. It should be noted that this is an issue that goes beyond fraudulent trading, or indeed insolvency law. Nowadays, the matter predominantly

---

510 As Davies notes, 'dishonesty' as a label is more evocative than 'knowledge': ibid 119.
511 [2002] UKHL 12.
512 ibid para 35.
513 *Attorney General of Zambia v Meer Care & Desai (A Firm)* [2007] EWHC 952 (Ch), para 347.

arises when dealing with liability for the dishonest assistance of a breach of trust.[514] The definition of fraud is largely context dependent[515] and therefore different standards of dishonesty are employed in particular cases.[516] A unified test, as such, is undesirable.[517] In the words of Shine, 'the level of culpability required in each case will depend on the origins and aims of the particular remedy sought'.[518] Thus, in short, it may well be that a quite different definition of dishonesty would apply in a case involving the dishonest assistance of a breach of trust, as compared with the definition applied in a case of fraudulent trading under section 213. It is argued that this has merely added fuel to the fire and exacerbated the level of confusion inherent within this area of law. As the author will now go on to uncover, considerable judicial energy has been expended upon determining the correct test and standard of dishonesty required in the civil context. This has in turn detracted from focus in other areas, ultimately leading to uncertainty, thereby further discouraging liquidators from bringing an action.

4.27 The primary issue has centred around whether a solely objective test should apply, whether subjective elements should also be considered and, if so, what precise level of subjectivity. Given the fragmented nature of dishonesty as a concept,[519] this has been approached in a variety of ways. In the criminal law, the working definition of dishonesty stems from the seminal case of *R v Ghosh*.[520] It requires that the jury first must find, according to the ordinary standards of reasonable and honest people, that

---

514 For an analysis of the cases in this area see Patricia Shine, 'Dishonesty in civil commercial claims: a state of mind or a course of conduct?' [2012] 1 JBL 29.
515 John Farrar, 'Fraudulent trading' [1980] JBL 336, 339.
516 Shine (n 514) 42.
517 *Re Patrick and Lyon Ltd* [1933] Ch 786, 790.
518 Shine (n 514) 42.
519 Ibid.
520 [1982] QB 1053.

what the defendant did was dishonest. If the first limb is answered in the affirmative, the jury must then consider whether the defendant himself must have realised that what he was doing was, by those standards, dishonest.[521] The later case of *R v Lockwood*[522], which *was* a fraudulent trading case, albeit in the criminal context, made it clear that the *Ghosh* test, it being of general application, also applied to fraudulent trading actions.[523] In other words, where a director in criminal proceedings takes the view that what he was doing was not dishonest, a jury must be directed to return a 'not guilty' verdict.

4.28 However, as has been alluded to, the position in the civil context is not as straightforward. This short analysis must begin with the Privy Council decision of *Royal Brunei Airlines v Tan*[524], a case, like many in this area, involving dishonest assistance of a breach of trust. Lord Nicholls acknowledged here that honesty 'has a connotation of subjectivity, as distinct from the objectivity of negligence'[525] and that dishonesty 'is a description of a type of conduct assessed in the light of what a person actually knew at the time, as distinct from what a reasonable person would have known or appreciated'.[526] It was made especially clear, however, that the decision as to what was considered dishonest conduct was for the court to make on an objective basis. Put simply, it is not for the respondent to set his own standards of dishonesty.[527] Shine suggests that following *Tan* 'it seemed clear that in equity, dishonesty could be

---

[521] ibid 1064.
[522] [1986] 2 BCC 99333.
[523] This decision was later met with approval by both the House of Lords and the Privy Council in two key civil cases, both dealing with the dishonest assistance of a breach of trust: *Twinsectra Ltd v Yardley* [2002] UKHL 12 and *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378.
[524] [1995] 2 AC 378
[525] ibid 389.
[526] ibid.
[527] ibid.

established without proof that the defendant believed himself to have been dishonest'.[528] However, the decision was reinterpreted by the House of Lords in *Twinsectra Ltd v Yardley*[529]. Indeed, much of the confusion and criticism in this area has stemmed from Lord Hutton's interpretation of *Tan* in that case.[530] In short, Lord Hutton in *Yardley* established the so-called 'combined test' for dishonesty in the civil context. In effect, it is the *Ghosh* test.[531] The combined test requires that two questions to be asked in order to find liability:

> (a) if 'the defendant's conduct was dishonest by the ordinary standards of reasonable and honest people'[532] and;
>
> (b) if so, did the respondent 'himself [realise] that by those standards his conduct was dishonest'?.[533]

As in *Tan,* this is caveated in that it is not for the defendant to set his own standards of dishonesty.[534] Thus, the *Yardley* decision, and the combined test of Lord Hutton, appears to represent the definitive position in law at the time of writing. It is worth noting that in the context of dishonest assistance of a breach of trust, however, further developments have been made and there is substantial new authority that suggests a move away from the subjective element imposed by Lord Hutton.[535] In the area of civil fraud however, the courts appear to have been content to apply, in unadulterated

---

[528] Shine (n 514) 31.
[529] [2002] UKHL 12.
[530] Not least by Lord Millett himself in the almost infamous dissenting judgment in *Twinsectra Ltd v Yardley* [2002] UKHL 12 itself.
[531] *Amgbah v Law Society* [2010] EWHC 2183
[532] *Twinsectra Ltd v Yardley* [2002] UKHL 12, para 27.
[533] ibid.
[534] ibid, para 36.
[535] For a substantial analysis of the development in the trusts context see Shine (n 514). In short, it would appear that the law in this context is moving away from the need to prove the subjective element of the test.

fashion, the combined test of Lord Hutton in *Yardley*.[536] As Shine notes, in light of the divergence of judicial opinion in relation to the appropriate test to use in differing circumstances:

> It is unsurprising that the court [in the context of fraud] has preferred a test which retains an element of subjectivity. This is an inevitable consequence of the gravity which attaches to a finding of fraud in a civil court. It is a very serious matter indeed to even plead an allegation of fraud, reflected in the onerous burden of proof imposed by the courts. The standard of proof is of course the balance of probabilities but, since the court must assume that fraud is so serious it must be unlikely…[j]udges in fraud cases are always concerned to not dilute the fault element inherent in an allegation of fraud[537]

It seems therefore likely that, due to the particularly serious nature of fraud, that it will be handled differently than other areas of civil liability where questions of dishonesty arise.[538] The result is that where a respondent 'honestly' believes that he did not act dishonestly, there can be no finding of liability under section 213.

4.29 The author's very terse summary of the present law does not do justice to the sheer uncertainty that has plagued the concept of dishonesty. It is in fact an unwieldy beast whose definition cannot be pinned down – in fact some judges have explicitly refrained from doing so[539] – and in the civil context it has become so vague and difficult a concept to handle that it is unsurprising that officeholders refuse to pursue potential claims in light of the overwhelming uncertainty. Indeed, as a result of the dishonesty requirement it is completely unsurprising that fraudulent trading is rarely pursued, but even more so that some commentators think of it as entirely insignificant in the context of the enforcement regime overall.

---

[536] See for instance *Aviva Insurance Ltd v Brown* [2011] EWHC 362 where it was found that the conduct had to be shown to be objectively dishonest, but also that the claimant had to prove the respondent himself was aware that he was acting dishonestly. In other words: the approach of Lord Hutton in *Twinsectra.*
[537] Shine (n 514) 40.
[538] *Aviva Insurance Ltd v Brown* [2011] EWHC 362.
[539] *Re Patrick and Lyon Ltd* [1933] Ch 786, 790

4.30 *Attribution and knowledge* The author here goes further, however, and suggests that a finding of dishonesty against the defendant, on a literal reading of the provision, is unnecessary. The incessant focus, in the case law, on the requirement under section 213(1) of dishonesty has often led to a sidestepping of the 'knowledge' requirement of section 213(2) which, it is argued, must be wrong in principle. It is generally accepted that knowledge is itself a prerequisite for a finding of dishonesty, i.e. a person who has knowledge of fraudulent activities is no doubt dishonest.[540] However, the legislation does not expressly require for this distinction to be made. It requires the recognition of an 'intention to defraud'[541] when 'any business of the company has been carried on',[542] but this intention to defraud is an intention that on construction must be capable of being attributed to the company itself. In other words, it is the *company* that is operating fraudulently and, as a corollary, dishonestly.[543] Where dishonesty cannot be attributed to the company, it is suggested that a respondent cannot be liable as section 213(1) is not engaged. As section 213(2) makes clear, it is mere 'knowledge' of the intention to defraud which must be found in the case of the respondent for liability to attach. The respondent is liable, by virtue of her knowledge, as an accessory to acts attributed to the company. The defendant herself may indeed be dishonest, or she may simply have knowledge of another's dishonesty, but in either case it is not necessary for the court to go as far as to make such a finding. This is of particular relevance given fraudulent trading's applicability to 'any person'. It must however be accepted that in close or

[540] *Morris v Bank of India* [2004] EWHC 528.
[541] IA 1986, section 213(1) .
[542] ibid
[543] For such an attribution, in line with general principles, it is therefore necessary that the individual who possessed the intent must have been the 'directing mind and will' of the company: *El Ajou v Dollar Land Holdings plc* [1994] BCC 143, 150.

owner-managed companies, this argument falls away as the distinction between the 'company' and the 'accessory' is eroded. But, it is submitted that, excepting those cases, it is not only wrong in principle that dishonesty has been introduced in this context, it is also often simply unnecessary to do so.

CONCLUSION

4.31 A series of substantive barriers to claims concerning both wrongful and fraudulent trading have been set out in this chapter. More importantly, in line with the purpose of this thesis, the author has demonstrated at least in part how the improper trading provisions struggle to achieve their underlying objectives – whether public or private. But, the author is hesitant to conclude fully in that regard at this stage, given that much of the analysis, and a number of other barriers to improper trading claims, fall to be discussed in the next chapter. That chapter will largely concern itself with the new assignment provision but, in doing so, it will by implication deal with in some detail the issue of *funding* improper trading claims, some further evidential difficulties, and the officeholder's ultimate dilemma: whether to risk the assets pot in commencing proceedings.

5

THE ASSIGNMENT OF INSOLVENCY ACT CLAIMS

5.1 In the context of IA 1986 claims, the most radical reform of the SBEEA 2015 is that which permits the liquidator or administrator (as the case may be) to *assign* an accruing cause of action. This new possibility,[544] brought to life by section 118 of the SBEEA 2015,[545] applies to both wrongful[546] and fraudulent trading,[547] as well as other[548] IA 1986 claims. Crucially, in addition to the action itself, any resultant proceeds may also be assigned.[549] The section thus permits, in effect, a circumvention of the *locus standi* requirements[550] which have been argued by this author in the previous chapter[551]

544 It has been made clear by the courts that, before the SBEEA 2015, an action under IA 1986 sections 213 or 214 could not be assigned by the officeholder: *Ruttle Plant Hire Ltd v SSEFRA (No. 3)* [2008] EWHC 730 (TCC); *Re Oasis Merchandising Services Ltd* [1995] 2 BCLC 493.
545 The provision was brought in to force by Regulations on 1 October 2015: The Small Business, Enterprise and Employment Act 2015 (Commencement No. 2 and Transitional Provisions) Regulations 2015, SI 2015/1689, reg 2(j).
546 IA 1986, s 246ZD(2)(b).
547 IA 1986, s 246ZD(2)(a).
548 This chapter only deals with those wrongful and fraudulent trading, though the section permits the assignment of a greater range of Insolvency Act powers, namely: transactions at an undervalue as (IA 1986, s 238); preference actions (IA 1986, s 239); and extortionate credit transactions (IA 1986, s 244). It should be noted that the T&T Discussion Paper (n 14) set out an original intention to exclusively allow wrongful and fraudulent trading claims to be assigned. Based on responses from the consultation, the Government instead widened the scope of the provision to permit it for other types of insolvency actions, see: T&T Government Response (n 223).
549 IA 1986, s 246ZD(2).
550 Although this is not the technical legal consequence, this is the practical effect. Crucially, however, it can only be done with agreement from the officeholder.
551 4.19

to be inhibitive of the overall success of the mechanisms. It might allow, for example, a pecunious creditor to step in, purchase the claim, and commence proceedings in their own right[552]. Alternatively, it permits a market to develop in insolvency claims bought by specialist companies.[553] A decision to assign may come about, for example, where the assets of the insolvent company are insufficient to pursue a claim; where litigation is imprudent in light of the potential chance for recovery; or where, for other reasons, assignment affords the best chance of realising the optimal value for company creditors by 'cashing in' for a swift return. At first blush, therefore, assignment appears beneficial. This chapter will continue the discourse of the previous one, though it will look more closely at some of the specific arguments surrounding assignment. Being the most crucial reform to the wrongful and fraudulent trading mechanisms since the IA 1986, it is clearly of considerable future importance for the regime as a whole, and therefore worthy of some interrogation. The chapter will therefore set out to determine the potential that assignment has for increasing the effectiveness of the fraudulent and wrongful trading mechanisms. It must be recognised by the reader that, at this stage, it is too early to determine the actual impact upon effectiveness and so the author only intends to examine its potential in this regard, more generally.[554] The previous chapter dealt with difficulties in the wrongful and fraudulent trading regimes more generally. It is indisputable that the introduction of assignment follows a recognition by the state of an existing problem with those mechanisms.[555] As a corollary, there must also be a

---

[552] With respect to fraudulent trading claims it should be remembered that, pre-1986, it was already the case that a creditor had standing: 4.19.
[553] Indeed, as will be discussed in due course, this was the very expectation of Government in making the changes: T&T Discussion Paper, 11.8.
[554] As explained previously: 1.12.
[555] T&T Discussion Paper, 11.2.

recognition that those mechanisms were not, at least in part, operating with optimal effectiveness, and thus not as successfully as now might be intended post-reform. It is therefore logical in that context to begin by setting out the *problem* that assignment allegedly serves to solve. In identifying the problem, the author can go further and set out whether it is likely to be successful in doing so, and thus have the intended effect of improving the overall effectiveness of the wrongful and fraudulent trading mechanisms. Ultimately, it will be concluded that assignment is unlikely to have anything more than a negligible impact in that regard. The author concludes that the number of wrongful and fraudulent trading cases brought to trial is unlikely to increase substantially, or even marginally, due to the substantive legal issues that exist in bringing a claim, and the matter of director impecuniosity; neither of which are affected by the assignment provisions. To the contrary, the evidence examined in this section uncovers a real danger of a rise in speculative or vexatious claims being brought against directors, some of whom may end up being pressured into settlement or left unable to defend themselves. It is therefore submitted that assignment may lead to an increase in the number of cases *settled*. It is also gingerly suggested that assignment may come to overtake (and thus replace, i.e. without a measurable increase in the number of cases) other methods of funding insolvency litigation following the costs ramifications introduced by the LASPOA 2012.

THE PROBLEM: FUNDING INSOLVENCY ACT CLAIMS

5.2 The reader has already been introduced to the DBIS *Transparency and Trust* consultation in a previous chapter.[556] It is the Discussion Paper arising out of this

[556] 2.32.

consultation ('the Paper') that led to, *inter alia*, the introduction of assignment. The Paper sets out the intended objectives of assignment as to: '[i]ncrease prospects of culpable directors being pursued where they have been responsible for allowing companies to trade wrongfully or fraudulently'[557] by giving the provisions 'more bite'.[558] It is unsurprising, then, that the rationale for the assignment provisions was said to be 'increase trust in our regime by ensuring that if directors…act fraudulently or recklessly they personally run the risk of being required to compensate those suffering loss as a result'.[559] Of course, this accords with the objectives of wrongful and fraudulent trading generally. The Paper asserts one of the core criticisms attributed to the mechanisms – that liquidators commenced proceedings infrequently – was 'largely because funds [were] not available'[560] A difficulty, it was said in the Paper, compounded as a result of the changes (at that time, proposed changes[561]) introduced by LASPOA 2012.[562] It is interesting to note that there is no mention in the Paper of the evidential and procedural difficulties faced by officeholders. Moreover, as Williams notes, it makes no suggestions dealing with other issues identified by commentators relating to the poor deterrent effect of the provisions.[563] Instead, on the author's reading, the problems with wrongful and fraudulent trading appear to be put down to a mere inability to fund

[557] T&T Discussion Paper, 11.4.
[558] ibid, 11.7.
[559] ibid, 11.4 (emphasis added).
[560] ibid, 11.2.
[561] Although the Act had been introduced by the time of the T&T Discussion Paper, a time limited carve out exemption for insolvency actions was in place by virtue of The Legal Aid, Sentencing and Punishment of Offenders Act 2012 (Commencement No. 5 and Saving Provision) Order 2013, art 4.
[562] The impact of this on insolvency actions will be considered in greater detail in due course: 5.7. See T&T Discussion Paper, 11.2. Which, for insolvency actions, came in to force on 6 April 2016 as a result of The Legal Aid, Sentencing and Punishment of Offenders Act 2012 (Commencement No. 12) Order 2016, art. 2.
[563] Williams, 'What Can We Expect to Gain from Reforming the Insolvent Trading Remedy?' (n 471) 63.

claims. Or, at the very least, this is the only issue substantively addressed by the Paper. The funding question is one that must therefore be explored in due course. But, at this juncture it should be said, when coupled with the introduction of compensation orders and undertakings to the realm of directors' disqualification, under the same Act,[564] Government trajectory for policy in this area seems to be not so much along the lines of prevention of misconduct, but rather in the increased regulation of directors, and a strengthening of the sanctions available to be utilised against them.[565] In examining the supposed funding difficulties in more depth, then, it is suggested the first step ought to be to consider what funding options have *previously* (i.e. pre-SBEEA 2015) been open to an officeholder in relation to fraudulent and wrongful trading claims.[566]

Do Nothing

5.3 Although not strictly a form of funding, it should be said initially that the IP, following an assessment of all of the evidence available to her, may simply decide to take no action. For example, due to the impecuniosity of the director concerned; due to evidential barriers; procedural issues; or otherwise. Alternatively, even where an IP determines there is a strong case to be made, she may be unable to commence proceedings on the basis that the funding options, discussed below, are unavailable or unworkable in that instance. It is the occurrence of this latter situation that the new assignment provisions attempt to mitigate against; by giving the officeholder a new alternative. Thus, in theory, assignment ought to increase the effectiveness of the

[564] 2.34.
[565] It will be argued in the next chapter of this thesis that this is, in fact, a misguided approach: ch 6.
[566] It should be noted that the forthcoming analysis only considers the primary options available to an officeholder where she is considering bringing specifically a wrongful or fraudulent trading claim. These actions differ from example, director misfeasance claims under IA 1986 s 212, or other miscellaneous contractual matters, such as director loan agreements, which have always been able to be sold or assigned.

wrongful and fraudulent trading provisions where it results in fewer cases of IPs opting to 'do nothing' simply on the basis of funding. Quite how often this occurs is a matter to be explored in due course.

Using the Assets of the Insolvent Company

5.4 Where there are sufficient assets in the insolvent company there is clearly little difficulty in initiating proceedings. However, this is no doubt rare given the nature of such companies as being impecunious. Another factor also falls for consideration in this regard. Wrongful and fraudulent trading actions are both personal to the liquidator or administrator. Therefore it is the sole right of that individual to bring an action, unless the claim is assigned under the new provisions.[567] Because of this, an officeholder commences proceedings in her own name and is personally liable for any costs (notwithstanding that she carries out her office for the benefit of the insolvent company or, when all is said and done, its unsecured creditors).[568] Where there is a shortfall in the company's assets, it falls to the officeholder to pay any difference.[569] Granted, whilst the IP will generally obtain an indemnity against the company in question to escape this difficulty, anecdotal evidence from practitioner members of R3 suggests that there is currently:

[567] *Re William C Leitch Brothers Ltd* [1932] 2 Ch 71; *Re Oasis Merchandising Ltd* [1995] BCC 911.
[568] The fact that insolvency practitioners carry out work in the public interest, yet receive no public funding for litigation (unlike, for example, with disqualification which is an entirely state funded mechanism) and, further, are personally liable for any debts incurred is a strange idiosyncrasy of English insolvency law. See the comments of Lord Millett in *Re Pantmaenog Timber Co Ltd.* [2004] 1 AC 158, [52] and Walton, 'The Likely Effect of the Jackson Reforms – an Empirical Investigation' (n 50) 10.
[569] For an in-depth discussion on this point see Chief Registrar Baister and Stephen Davies, 'Liability of Insolvency Practitioners for the Legal Costs of Litigation' (May 2009) <http://bit.ly/2b21B3C> accessed 01 July 2016, para 36. It is interesting to contrast the position of the liquidator from that of the Official Receiver who benefits from immunity: *Mond v Hyde* [1999] QB 1097.

> [A] widespread practice of directors leaving insolvent companies with no or virtually no assets. These companies have no assets with which to fund an investigation into directors' conduct…[and]…there is no money with which to fund any litigation[570]

Therefore, given the personal risk attached it is suggested that IPs will avoid funding litigation in this way, except where no other viable option presents itself, and there is a very strong likelihood of success. Thus, although distasteful, the author notes that any would-be miscreant director might be well-advised to go about 'milking the company dry' before plunging it into an insolvency regime, so as to reduce the options open to the officeholder in investigating and pursuing any misconduct.[571]

Using a Litigation Funder

5.5 It has been argued by Crinson and Morphet that, where the assets of the insolvent company are insufficient, creditors should be 'the first source of funding [the officeholder] should consider'.[572] However, it is submitted that creditors will be cautious of 'throwing good money after bad', thereby exacerbating their losses, save in circumstances where the likelihood of recovery is extremely high. There is also anecdotal evidence to suggest that the vast majority of creditors (generally smaller concerns) often play no part in insolvency proceedings.[573] Indeed, some companies – and the author is particularly mindful of those who suffer a 'domino' insolvency arising from misconduct – will almost certainly have no inclination, or even the financial

[570] Walton, 'The Likely Effect of the Jackson Reforms – an Empirical Investigation' (n 50) 11.
[571] This was the very 'advice' given, over two decades ago, to directors seeking to avoid liability by some commentators. See Christina Williams and Andrew McGee, *A Company Director's Liability for Wrongful Trading* (ACCA Research Report No. 30, 1992), 13.
[572] Katharina Crinson and Sophie Morphet, 'Funding for actions brought by insolvency officeholders' (2011) 24(7) Insolv Int 108, 110.
[573] This was the view of the Fraud Advisory Panel in its submission to the Department for Business, Innovation and Skills as part of the Transparency & Trust consultation. The FAP contended that smaller creditors are often 'ill-informed and do not participate [in wrongful and fraudulent trading proceedings]'. A ZIP archive containing all such responses is available at <http://bit.ly/2bM33GU> accessed 01 August 2016.

ability, to fund further uncertainty. However, creditor funding, in some circumstances, may be an optimal solution; for instance, where a larger creditor is able and willing. But, in reality, it is unclear how often this occurs. There is evidence to suggest that HMRC, in its capacity as unsecured creditor, has in the past funded such actions. Given that the Revenue is invariably the largest unsecured creditor of an insolvent company it clearly has a vested interest in ensuring that proceedings are taken, where possible, with a view to recovery for the tax payer. Funding from the HMRC at present however has been described as 'significantly restricted'[574]. But, any awards made following creditor-funded actions still have to be distributed amongst the *entire* pool of creditors, and the individual funder would not be able to demand a higher proportion in view of her contribution.[575] As such, this option seems to this author likely to be pursued only either where the creditor concerned is owed the bulk of the unsecured debt of the company; is acting in a public interest capacity, as with HMRC; or where, for whatever reason, an opulent creditor pursues litigation on a point of principle. In default of creditor funding, the officeholder may seek the services of an independent third-party 'litigation funder' who will provide funding in consideration for any eventual proceeds. It has been said, however, that this type of funding is often expensive and difficult to obtain, as at least a 70 per cent chance of success will be demanded by the funding party.[576]

---

[574] Walton, 'The Likely Effect of the Jackson Reforms – an Empirical Investigation' (n 50) 15.
[575] Indeed, doing so could engage issues of champerty and maintenance. For an historical exposition of those rules in the insolvency context see Crinson and Morphet (n 572). The largest insolvency litigation funder in the UK, Manolete Partners plc, however, contends that it can provide funding solutions that fall outside the scope of the champerty and maintenance rules. The market has adapted to overcome this particular limitation, so it would seem. See Manolete Partners Plc, 'Frequently Asked Questions' <http://bit.ly/2bQMSdl> accessed 01 August 2016
[576] Crinson and Morphet (n 572) 110.

Using CFAs and/or ATE Insurance

5.6 The methods of funding explored thus far exhibit obvious difficulties for the officeholder; creating a lacuna which assignment may indeed fill. However, since July 1995 an officeholder has been able to work alongside a solicitor or specialist firm to pursue cases by means of a CFA.[577] This solution is most useful where there are some assets within the insolvent company, to cover legal fees and insurance premiums, though not enough for the officeholder to commence proceedings on her own. In companies that have been 'milked dry' and where third-party litigation funding is unavailable, this will invariably be the only other way in which litigation can be brought. In fact, according to anecdotal evidence, the vast majority of insolvency actions (i.e. pre-SBEEA 2015) take place in this way; perhaps upwards of 90 per cent.[578] Of course, as with litigation funders, solicitors and counsel are only likely to be retained on a CFA basis where there is a good chance of the action succeeding. The claim is still brought in the name of the officeholder. As a result, the original problem of funding is returned to: although the officeholder may have minimised her own legal costs by the use of a CFA, she can still be liable personally for any *adverse* costs orders made should the action fail. Because of this, she will seek specialised After The Event (ATE) insurance to protect herself in the event of failure.[579] It is possible to utilise ATE

[577] Highly popularised by personal injury claims, this type of agreement involves engaging a solicitor or other authorised claims firm for fees less than the standard rate where the action fails. A successful action, however, will usually require paying fees at the standard rate, plus an additional 'success fee'. They were first introduced by the Court and Legal Services Act 1990, s 58. However, it was not until the Conditional Fee Agreements Order 1995 that the first 'no-win, no-fee' type arrangements were made available for insolvency litigation.

[578] DBIS, 'Impact Assessment: Enabling Liquidators and Administrators to assign to third parties certain rights of action that only they can bring under the Insolvency Act 1986 and to extend to the right to bring fraudulent and wrongful trading actions to an administrator' (BIS INSS007) available at <http://bit.ly/2c2UtnE> accessed 01 August 2016, para 11 (Assignment Impact Assessment).

[579] It is also extremely noteworthy that under CPR 25.13 the defendant in, *inter alia*, wrongful or fraudulent trading proceedings may obtain an order for security for costs where it is thought that the

insurance as a standalone product, for instance where the company has sufficient assets to start proceedings but may not have enough to defend against an adverse costs order, or where the defendant seeks a security for costs order. However, by far the most common usage of ATE insurance is when combined with CFAs. ATE insurance will typically cover any adverse costs orders and the officeholder's own disbursements including a proportion of legal fees if the case is lost. Generally, a premium is only payable to the insurer where the case is won, otherwise the insurer receives nothing.[580] Originally, it was the insured *officeholder* who was liable to pay the ATE success fee where she won her case; she could not recover it from the losing party as she could her ordinary costs. In April 2000, however, legislation led to a change in this position.[581] Thereafter, successful parties were able to recover from the opposition any success fees and ATE premiums *in addition* to ordinary costs, thus enhancing returns for creditors.

5.7 However, as a result of a serious review of civil litigation costs by Jackson LJ,[582] culminating in the introduction of the LASPOA 2012 ('the Jackson Reforms'), from

---

officeholder will be unable to pay them due to the nature of the company's insolvency. The fact that a company is in liquidation is prima facie evidence that it will be unable to pay costs, unless of course it can be proven otherwise: *Smith v UIC Insurance Co Ltd* [2001] BCC 11; also see Jackson LJ (ed), *Civil Procedure: The White Book Service 2016* (Sweet & Maxwell, 2016) 25.13.14 (The White Book). One way of doing so is being the holder of a comprehensive ATE insurance policy. It is therefore, practically speaking, mandatory that officeholders obtain such a policy before commencing an action, if the company has limited assets. See recently *Premiermotor Auctions Limited v PricewaterhouseCoopers LLP and Lloyds Bank plc* [2016] EWHC 2610 (Ch), where Snowden J ruled that the existence of an ATE insurance policy meant the threshold for a security for costs order was not met. R3 has reported that it is common for a defendant to ask the court to dismiss proceedings, on the basis of inadequate cover for adverse costs, where no ATE insurance is in place: Walton, 11. This creates the repugnant, though somewhat interesting, situation where a fraudulent or badly behaving director who has 'milked the company dry' can then attempt to have any proceedings taken against her struck out on the grounds that the company is impecunious.

580 See e.g. Crinson and Morphet (n 572) for more technical detail as to how ATE insurance operates.

581 Access to Justice Act 1999, s 29.

582 The Stationary Office, 'Review of Civil Litigation Costs: Final Report' (December 2009) available at <http://bit.ly/1IkgolZ> accessed 01 August 2016.

April 2016[583] it is no longer possible for officeholders to recover these. Instead, any CFA/ATE insurance fees paid must be deducted from the main award.[584] In fact, one of his Lordship's main areas of criticism in this wide-ranging review focused on the use of CFAs and ATE insurance in civil litigation.[585] The post-2000 (but pre-Jackson Reform) position was described by Jackson LJ as being unsatisfactory for the following reasons:[586]

> (a) the claimant may be operating at no risk as to costs, through the combined use of CFAs and ATE insurance. The claimant will pay no costs whether she wins or loses.
>
> (b) the defendant, on the other hand, may be litigating at a massive costs risk. She may be liable for up to four times the costs of the action: her own costs; the claimant's ordinary costs; the claimant's CFA uplift; the claimant's ATE premium.

5.8 His Lordship, in short, sought a change in the law to ensure a 'level playing field'[587] for both the claimant and defendant, 'rather than one sloping at 90 degrees'.[588] Thus, since the implementation of the Jackson Reforms, any CFA uplift and/or ATE premiums must be deducted from the amount of damages awarded. This has the result of insulating the defendant from a 'massive costs risk'.[589] Though, of course, a by-product is to reduce the overall pot for the insolvent company's unsecured creditors.

---

[583] Whilst his Lordship recommended that these reforms be implemented across all areas of civil litigation at the earliest opportunity, the Government specifically exempted actions brought by office holders, on a temporary basis. Originally, the exemption was due to come to an end in April 2015: see the written Ministerial Statement by Jonathan Djanogly at HC Deb 24 May 2012, col 94W. This was later extended to April 2016: see the written Ministerial Statement by Dominic Raab: HC Deb 17 December 2015, col 420W. The result is that, at the present time of writing, the full effects of the LASPOA 2012 are in force in relation to officeholder-founded actions.

[584] As a result of the LASPOA 2012, s 46 which amends the Courts and Legal Services Act 1990 to create s 58C.

[585] The Stationary Office (n 582) para 2.1-2.2.

[586] Jackson LJ, 'The Civil Justice Reforms and Whether Insolvency Litigation Should Be Exempt' (The Mustill Lecture, Leeds, 16 October 2015) available at <http://bit.ly/1RRLHap> accessed 01 August 2016, para 2.3.

[587] ibid para 7.4.

[588] ibid.

[589] ibid para 2.3.

Indeed, a situation might readily arise in which creditors of the company see no return whatsoever, even where the officeholder is successful. Once the legal costs, the officeholder's own fees, and any ATE premiums have been stripped away, very little may remain. In particularly small estates, it is conceivable that the officeholder or her legal team might not receive full payment of any fees due. For these reasons, amongst others, it has been thought for some time that the Jackson Reforms will cause substantial shockwaves for officeholders considering taking action against directors.[590] It is still too soon to gauge any real-world impact. However, the new position has been strongly criticised by many of those in the insolvency sector,[591] as well as the Bar Council.[592] Much of the criticism in the literature is founded upon an empirical study conducted by Professor Walton, on behalf of R3.[593] Walton in his analysis argues that the introduction of the reforms will mean that fewer cases are brought, particularly at the lower end of the scale.[594] For those that are brought, he argues, more will go to trial as a result of their being less incentive for directors to settle given their lessened exposure to potential costs orders.[595] This is because it is a feature of ATE insurance that the premium is staged so that it increases at milestones in the litigation. It has been reported anecdotally that this has proven to be a useful tool in pressuring defendants to settle at an earlier stage; they being fearful that the longer they 'resist' the more costs incurred should they lose at trial. Walton has even gone as far to say that the Jackson Reforms are 'likely to

---

[590] For a comprehensive critique of the introduction of these reforms in to the insolvency arena see Walton, 'The Likely Effect of the Jackson Reforms – an Empirical Investigation' (n 50) 11.
[591] Not least, of course, by Walton, ibid; Walton, 'Insolvency Litigation and the Jackson Reforms – An Update' (An R3 Report, April 2016) <http://bit.ly/1SO0cLE> accessed 01 July 2016, 2.3.
[592] See, for example, Sarah-Jane Bennett, 'The Legal Aid, Sentencing and Punishment of Offenders Act 2012 (LASPO): One Year On, Final Report' (A Bar Council Report, September 2014) available at <http://bit.ly/1vzRMwT> accessed 01 August 2016, para 230.
[593] Walton, 'The Likely Effect of the Jackson Reforms – an Empirical Investigation' (n 50).
[594] ibid 46.
[595] ibid 32.

encourage more culpable behaviour by bankrupts and directors'[596], contrary to one of the underlying objectives of the improper trading provisions as being to deter misconduct. Walton estimates that creditors, including the HMRC and small businesses, collectively may be more than £160 million worse off per year as a result of the changes.[597] Crinson and Morphet, in 2011, adopted a more optimistic stance. They argued that the changes would simply cause the market to 'respond with revised packages'.[598] They described the litigation funding market as being 'on the brink of change'[599] with it responding to the new legislation with 'innovative and competitive products which [would] open up funding opportunities to insolvency office holders'.[600] They ultimately concluded that the 'reforms mean that the next year or so will be an exciting time for litigation funding'.[601] The point is, put simply, that markets adapt. As expressed previously however, the later accounts, from those such as Walton, hail it as being a far cry from a time of excitement. Interestingly, what Crinson and Morphet could not foresee was the game-changing introduction of the assignment of actions to this area.

5.9 Despite the steadfast praise of those such as Walton, it is important to remember however that the use of CFAs and ATE insurance is by no means the holy grail of insolvency litigation 'funding'. Many insurance policies suffer their own significant limitations and as a result, even where a CFA/ATE approach is a viable option, an office

[596] ibid 46.
[597] ibid 29. This is also a point picked up, in critique, by Jackson LJ. His Lordship refutes this, arguing that '[Walton's] report simply does not support that proposition': Jackson LJ, para 8.12.
[598] Crinson and Morphet (n 572) 111.
[599] ibid.
[600] ibid.
[601] ibid.

holder may be seriously deterred from commencing proceedings. Some of the recognised issues with ATE insurance are:

(a) as noted by Crinson and Morphet one of the most significant is that it does not create a cash flow for the officeholder.[602] Therefore in order to commence proceedings counsel and solicitors must agree to have their payment of fees deferred until the insurance policy pays out.

(b) it is expensive, with premiums of between 50 and 110 per cent of the insured amount;

(c) due to the scarcity of insurance providers and the technicalities of each individual policy, they take many months to organise. This results in a longer liquidation/administration process, and therefore increases costs;

(d) once a policy is taken out, the office holder must be careful to constantly update the insurer with details as to how proceedings are progressing, otherwise cover may be invalidated;

(e) there is a risk that the insurer will seek to avoid paying out under the policy, leading to severe financial consequences for the office holder; possibly her own insolvency;

(f) the premium paid on the policy is top-sliced from any return, potentially leaving the office holder and their lawyers unpaid in the case of a small award. More importantly, a situation might occur whereby an office holder is successful but delivers zero return for creditors due to the cost of the premiums as against the award made.

Despite the disadvantages of the insurance approach, the combined use of CFAs/ATE appears to have nonetheless become totally dominant in this area.[603]

IS FUNDING ACTIONS STILL A PROBLEM?

5.10 Exploring the existing funding mechanisms has in fact uncovered a significant point for observation. Although it is indisputable that each suffers its own (sometimes significant) deficiencies, it is somewhat surprising that the Paper appears to have laid

[602] ibid.

[603] Walton, 'The Likely Effect of the Jackson Reforms – an Empirical Investigation' (n 50) Executive Summary.

all of the inadequacies of wrongful and fraudulent trading on funding concerns. Indeed, despite the Government's claim that it is a considerable burden for officeholders, they present no empirical evidence, or in fact *any* evidence, save for anecdotal, to that effect. The only empirical studies that this author can find on the subject are those, dealing specifically with wrongful trading, published by Williams and McGee in 1992,[604] and Andrew Hicks in 1993.[605] Williams and McGee commented that '[t]he reality is that by far the biggest consideration is the question of costs';[606] alluding to the fact that funding is perhaps of a greater concern than the substantive legal issues.[607] Hicks, on the other hand, was far more direct in stating that '[i]t is clear that the greatest inhibition to wrongful trading claims is the cost of investigating and then pursuing the claim'.[608] In terms of the research conducted across both of these studies, there are four important factors to consider. First, the studies here are old. Second, the sample sizes were small. Third, the methodology in both cases was to obtain information by way of interview. Williams and McGee interviewed a broad range of professionals including accountants, solicitors, insolvency practitioners and bank officials.[609] Hicks interviewed accountants, solicitors and IPs.[610] Fourthly, the time at which the interviews were conducted, and the studies published, was before the CFA existed – clearly a game-changer for officeholders. Much of the modern rhetoric surrounding the funding crisis in this area is hinged upon these out-of-date and solely anecdotal accounts. What is suggested here

[604] Williams and McGee (n 454).
[605] Andrew Hicks, 'Wrongful trading – has it been a failure?' (1993) 8(5) IL&P 134.
[606] Williams and McGee (n 454) 13.
[607] It is assumed here that Williams and McGee mean 'costs' to include both those needed to investigate and pursue directors, but also adverse costs in the case of failure.
[608] Hicks, 'Wrongful trading – has it been a failure?' (n 605).
[609] Williams and McGee (n 454) 2.
[610] Hicks, 'Wrongful trading – has it been a failure?' (n 605).

is that, although there are clearly funding issues in the narrow sense that the insolvent company *itself* is generally unable to cover the costs of insolvency litigation, the market has adapted and a range of products and services have been established to aid officeholders in cases that are viable, following the introduction of CFAs. Whilst funding concerns *may* have been the first – and invariably an insuperable – obstacle for officeholders pre-1995, it seems plausible that the substantive legal issues have since trumped funding claims as being the main inhibitor. Aside from this outdated empirical data, there does not appear to be anything that would suggest a great funding crisis exists. Although it is accepted that an absence of evidence is not evidence of absence, it is altogether simply unclear upon what evidence the claims in relation to funding, as set out in the Paper, are based. In truth, this is a matter difficult to satisfy without an up-to-date widespread empirical study. If such a study has been concluded, no reference was made to it in the Paper. Moreover, it is the author's view that the advent of more modern funding options has rendered any such arguments far less potent than they might formerly have been. The simple point being made here is that too much time is spent on the oft regurgitated concerns about funding, based upon outdated evidence. Purporting to address a problem that does not exist (or is of marginal concern) by definition will not serve to increase the effectiveness of the IA 1986 private enforcement powers. In fact, it may reduce their effectiveness in the long term if its focus detracted from other material concerns. It is argued that unless further evidence to substantiate the funding dilemma is forthcoming, then it is time to move on and address the other, more inhibiting, issues that remain.

ASSESSING THE *TRANSPARENCY AND TRUST* CONSULTATION

5.11 DBIS released its *response* to the *Transparency and Trust* consultation process in April 2014. In forming its conclusion that assignment was to be introduced, DBIS considered some 314 consultation responses from companies, NGOs, professional and trade associations, academics, enforcement agencies, and individuals.[611] The author obtained all of these responses[612] and has analysed them for the purposes of obtaining some insight as to views on the potential utility of assignment. In DBIS's own words:

> Most respondents agreed that very few fraudulent trading and wrongful trading actions are currently taken by liquidators…[v]iews were more mixed on the proposal to make it possible to sell or assign actions to third parties.[613]

Out of the 314 consultees, 116 wrote on behalf of corporations, NGOs, government agencies and academics.[614] The remaining 198 wrote in their capacity as private individuals. Five of the responses from individuals were unobtainable and so had to be excluded from the analysis.[615] It must be noted that, given the wide-ranging remit of the consultation, only a fraction of consultees considered the matters associated with creditor redress. A total of 45 non-individuals and a mere 3 individuals[616] wrote to the Department to discuss matters surrounding creditor redress. The limitations of the

---

[611] DBIS, 'Consultation Outcome – Company ownership: transparency and trust discussion paper' (15 July 2013) available at <http://bit.ly/1nD5QSo> accessed 1 August 2016.
[612] 111 of these submissions were available within a ZIP archive on the DBIS website, available at <http://bit.ly/2bM33GU> accessed 01 August 2016. The remaining consultation responses were obtained under the FOIA 2000 from DBIS (T&T Consultation Responses).
[613] T&T Government Response (n 223) paras 263-264.
[614] For the purposes of brevity these consultees will collectively be referred to as 'non-individuals' hereinafter.
[615] These responses were withheld by DBIS under Freedom of Information Act 2000 (FOIA 2000), s 41, on the basis that their release might amount to a breach of the duty of confidence that was owed to those particular respondents.
[616] One might draw from this, albeit quite unscientifically, that the general public at large considers creditor redress as being an issue of minimal importance. Conversely, it is interesting to note that 99 per cent of individual respondents discussed issues surrounding the Government's proposed register of beneficial owners of companies. Further, 98 per cent of individual respondents solely discussed this issue in their response.

sample size of this study therefore should be borne in mind. That notwithstanding, it is suggested the insight is important. It is rare to be able to obtain views from such a broad cross-section. There is also great value in that many of the respondents have first-hand practical experience of the concerns faced.

Questions Asked

5.12 Consultees were asked to consider a variety of questions on the topic of the use of assignment to improve financial redress for creditors.[617] This analysis concentrates on two of the core questions which assist the author in furthering his exploration of the effectiveness of the fraudulent and wrongful trading mechanisms. More specifically, in order to ascertain the impact that assignment may have in that regard. The questions considered here are:

(a) '[w]hether this proposal would improve confidence in the insolvency regime?';[618] and

(b) '[w]hether, if liquidators were able to sell or assign wrongful and fraudulent trading actions, more actions would be taken?'.[619]

The Results

5.13 It should be noted that a total of *zero* private individuals responded to either of the two questions. Dealing with the first question, there were 27 non-individual responses. Despite being one of the primary aims of the SBEEA 2015, it is interesting to note that only four (14.8 per cent) consultees definitively thought that it would. In a further three (11.1 per cent) responses, the author was able to infer with some certainty that the consultee thought that it would do so, though without it being explicitly stated.[620]

[617] T&T Discussion Paper (n 14).
[618] ibid, para 11.12.
[619] ibid, para 11.12
[620] Whilst this is admittedly somewhat unscientific, the author took a common-sense approach, by considering factors such as the content and tone of the response, and so forth.

This is in stark contrast to the 11 (40.7 per cent) respondents who were of the opinion that it would not increase the confidence of stakeholders in the insolvency regime, with this being inferred in a further seven (25.9 per cent) responses. Interestingly, two consultees believed that it would have the opposite effect and would in fact *reduce* confidence in the regime. The reasons for this will be examined in detail in due course[621] though can be summarised at this stage as being due to the potential for speculative or vexatious claims being pursued by commercial entities; and the potential for a negative public perception of corporations profiting at the expense of aggrieved creditors.

5.14 The results in response to the second question are more difficult to comprehend. It should be noted that the sample size here was much lower, with only 15 non-individual (and again zero individual) consultees engaging. This was expected as, in truth, it is more or less impossible to gauge the numerical impact of assignment on the cases brought at this stage.[622] For present purposes it is noteworthy that, including where it could be inferred from the totality of the response, a total of 8 (53.3 per cent) consultees thought that it *would* increase the number of actions brought. However, a proportion of that total, some 37.5 per cent, suggested that any increase would be in speculative or frivolous claims made by claims companies in an attempt to coerce the director (or other defendant) into settlement.[623] Seven consultees (46.6 per cent) who answered this question thought that assignment would not increase the number of cases brought. Six of those attributed that to the fact that the low number of cases was a result of the substantive legal difficulties, rather than funding concerns. This corroborates the

[621] 5.19.
[622] 1.12.
[623] Dealt with substantively below: 5.19.

author's suspicions expressed earlier in this regard. Given the responses, it is now therefore doubly unclear as to why DBIS insisted that funding was perceived to be the primary obstacle. And, even following this cursory examination, it is surprising that DBIS chose to use the word 'mixed'[624] to describe the appetite for assignment amongst consultees, and its potential to increase trust in the insolvency regime. It seems rather clear to this author that, in the main, assignment was not particularly favoured. The underlying reason for this, it is repeated, is simply that assignment does not necessarily solve any real problem. In fact, as will be explored below, it may cause more difficulties than it will solve.

THE PITFALLS OF ASSIGNMENT

5.15 To summarise, then, the primary benefit of assignment in policy terms lies in its potential to reduce the number of instances where an officeholder is unable to proceed with an action against a director due to funding constraints. This increase should have a proportionate impact upon the returns to unsecured creditors, thus enhancing the effectiveness of the mechanisms. It may also lead to wider reporting of such cases – whether in the law reports or the media – and therefore operate so as to increase the deterrent effect of the legislation.[625] Though it has been queried by this author, in line with the scepticism of *Transparency and Trust* consultees, whether the perceived benefits will be realised on the basis that there is no real evidence to support the notion that a funding crisis exists. Further, the likelihood is that where claims are not pursued,

[624] T&T Government Response, para 264.

[625] This is a point central to the author's suggestion for reform as dealt with later in the thesis: education leads to awareness, which in turn leads to deterrence: 6.20. The importance of deterrence in this area has also been considered by those such as Andrew Campbell, 'Wrongful Trading and Company Rescue' (1994) 25 Cambrian LR 69, 81 and Williams, 'What Can We Expect to Gain from Reforming the Insolvent Trading Remedy?' (n 471) 62.

in a market dominated by the CFA, it is for reasons other than issues of funding. That notwithstanding, assignment also carries a number of other supplementary benefits, such as preventing the officeholder from being exposed to personal liability, therefore eradicating the need for expensive ATE insurance policies. However, an analysis of the *Transparency & Trust* consultation responses reveals a considerable number of potential pitfalls that may seek to limit the positive impact that assignment could have. The next section sets out some of the concerns that were identified during the course of the analysis. The point being made is that even it can be shown that assignment alleviates funding issues (i.e. we accept the crisis is 'real'; which is disputed), it may create other adverse consequences that outweigh any of its positive effects, thus hindering the effectiveness of the regime overall.

Difficulties in Obtaining Information

5.16 Officeholders benefit from powers of investigation conferred by statute under, *inter alia,* sections 235-237 of the IA 1986. These compel those connected with insolvent companies to cooperate with the officeholder and, further, to furnish her with any documents relevant to the activities of the company where required. Evidently, in building any wrongful or fraudulent trading case against an individual, access to such documentation is vital. Given the nature of the forensic examination that needs to be undertaken where impropriety is suspected, claims are unlikely to succeed should such unrestricted access to documents be unavailable. These powers are unavailable to non-officeholders, even in the case of assignment. Because of this, there seems little doubt that an essential characteristic of any assignment agreement would be that, where the assignee requires investigations to be undertaken, this would be done by the officeholder for a fee.[626] This presents difficulties as, given the nature of the officeholder's duties to creditors, it may be seen to be detrimental on policy grounds that an Officer of the Court might be motivated by the objectives of a commercial third party, rather than creditors. It would be an injustice to the insolvency profession to suggest that this would actually occur in practice, but the perception might exist nonetheless, thus in turn reducing trust and confidence in the regime. There are also inherent difficulties of policy with quasi-public powers being used to this end. Depending on the circumstances, it is possible that it may amount to a breach of the officeholder's obligations to creditors. However, without contractual assurances that the officeholder will undertake investigations on behalf of the assignee it is unlikely that an agreement would be entered in to, thereby providing no net benefit to creditors whatsoever. It is noteworthy that, of course, under a CFA/ATE arrangement this presents no problems as the officeholder retains property rights in the action and any proceeds.

***De Facto* Settlements**

5.17 A number of consultees warned of the danger that potential defendants, or connected persons or entities, could simply buy out claims against them, so as to ensure that litigation could not ensue. This is more than a remote possibility. After all, a potential defendant is the one who is best placed to know the 'value' of any claim against her, as well as the likelihood of its success. She will have been inextricably tied to the activities of the insolvent company; she would know the extent of her wrongdoing, the availability of the evidence to the officeholder, and the monetary worth

[626] Whilst methods vary from funder to funder, Manolete Partners PLC – the largest UK insolvency litigation funder – operates in this way.

to creditors of any wrongful or fraudulent trading that she has been a part of. Even if the officeholder in question refused to make an assignment to the defendant herself it would be very straightforward for an SPV to be established, or for some person connected to the individual (perhaps a friend) to purchase it. Post-assignment an officeholder would have no recourse and, even with the best due diligence, it would be very difficult to detect and prevent in the first place (if prevention is desirable). Such a scenario amounts to a *de facto* settlement which, it might be argued, provides a better return for creditors than nothing at all, should the alternative be that no action is taken by the officeholder herself. However, one consultee commented that the public perception of *de facto* settlements would be negative and it may diminish trust and confidence in the enforcement regime itself. This argument is persuasive, and is compounded by the fact that, given what has been said previously, it is very likely that the cases in which a director is eager to purchase a cause of action are cases worthy of the officeholder pursuing. If this transpires to be a reality, the effectiveness of private enforcement mechanisms are, it is argued, diminished on two grounds. First, because it may lead to less of a return for creditors in otherwise actionable cases. Secondly, it further damages the deterrent effect should directors come to learn that this might be an option as it permits them to 'buy their way' out of sanctions, possibly at a rock bottom price. DBIS acknowledged these dangers in its Response[627] though, in spite of calls from consultees to ban assignment to defendants or connected persons, this did not make it to the legislation. DBIS commented that it was for officeholders, given their skill and experience in insolvency matters, to ensure that assignees were appropriate.[628] Although

[627] T&T Government Response, para 265.
[628] ibid, para 272.

laudatory this is unlikely to be of much comfort to officeholders or creditors. By way of mitigation an officeholder might decide as a matter of her own policy only to sell to creditors or recognised claims companies. However, therein lies a further issue: should there be no potential purchaser other than the director, might an officeholder have no choice but to assign should she be made an offer even for a nominal sum? Although the officeholder has an absolute discretion to assign – at least in theory – in practice if she refuses, there may at least be an argument that she has breached her duties to creditors to maximise returns for the insolvent estate. The officeholder may be put under considerable pressure from creditors to go ahead with the assignment. Granted, such a scenario is likely to be incredibly rare given that, if the claim was credible and no purchaser was available, the officeholder would pursue it herself by means of a CFA/ATE arrangement. However, it is not beyond the imagination.

Valuing Claims: The Bird in the Hand or the Two in the Bush?

5.18 One practical concern for the officeholder in assigning is determining the worth of a claim. This may be extremely difficult in the early investigative stages. R3, in its submissions to the *Transparency & Trust* consultation, commented that it is common for evidence that may be used against a director to 'drip' through as the investigation proceeds.[629] At the outset, before formal investigations have been concluded, the monetary worth of a claim may not be possible to gauge with certainty. One of the negative consequences of assignment is that, given the innate risk in commencing proceedings, claims companies are likely to only pay a fraction of its estimated worth. This has the effect of reducing the pot available to creditors. This is further compounded

[629] T&T Consultation Responses

by the fact that claims companies are only likely to be interested in the more 'valuable' claims in the first place. Where the action succeeds, they are likely the only party to benefit substantially from a windfall award. This is because, in view of the difficulties surrounding valuation, claims companies will seek to undervalue claims to further maximise profit. At the early stages, the officeholder is unlikely to be in particularly strong negotiating position; she has carried out only cursory investigations; the litigation funder is acutely aware that the claim is unlikely to be pursued without their financing; and, ultimately, the officeholder is duty bound to maximise returns for creditors. Whilst it might be argued that an officeholder could choose to assign later down the line, once investigations have been concluded, this suffers from its own difficulties. An officeholder is unlikely to commit to a forensic examination of a potential defendant, at significant cost, before funding arrangements are in place, so as to avoid wasting the already limited resources of the insolvent estate. In theory, this is a simple economic exercise for the officeholder, though the reality is no doubt far more complex. The option to assign will invariably present itself in cases where chances of recovery are high and/or the value of the claim is particularly healthy. A decision to assign is therefore inevitably going to be a worse trade-off for creditors than if the officeholder were to pursue to claim for herself. It may therefore be said that this hinders the effectiveness of the enforcement mechanisms by providing less of a return. However, this is arguably a better scenario than no case being brought whatsoever due to funding constraints.[630] This must be balanced against any negative public perception vis-à-vis commercial entities profiting at the expense of aggrieved creditors. In the

[630] Immeasurably more so when it is considered that this is Government's primary rationale for introducing assignment.

words of one consultee: does the officeholder take the decision to have a bird in the hand rather than the two in the bush?

Speculative, Nuisance and Vexatious Claims

5.19 It was a further concern that assignment may do little more than increase the number of speculative claims brought against directors. It would be certainly undesirable for a culture of barratry to emerge with regards to insolvency actions but this is a very real danger. Whilst it was freely admitted by Government that it would expect a 'market' surrounding these claims to emerge,[631] there was no acknowledgement or further discussion with regards to nuisance claims specifically. This is an issue peculiar to assignment because of the duties owed by officeholders to creditors. Commercial entities, as potential assignees, on the other hand are invariably driven by profit. The danger is therefore that even the weakest of claims could be bought cheaply from officeholders, who may be pressured or even duty bound to accept. Assignees would then seek to procure, under threat of litigation, a settlement from directors even where there is limited evidence of any wrongdoing.[632] Directors of insolvent companies, many of whom will have given personal guarantees to secure company debt, may not have the funds to defend the claim and will simply fold under the pressure.[633] Directors

[631] T&T Discussion Paper (n 14) para 57.

[632] This is also a serious concern in respect of another SBEEA 2015 initiative, namely compensation orders and undertakings: 2.34.

[633] Importantly, it is this very concern that Jackson LJ had in relation to the use of CFA/ATE insurance in civil litigation. This was aired in the Supreme Court in *Coventry v Lawrence* [2015] UKSC 50, where the practice of doing so in general terms was described as a 'blackmail' or 'chilling effect', 'which drove parties to settle early despite good prospects of a defence' at [43]. The potential for undue pressure to be placed on defendants was also a reason cited for the change in the law relating to fraudulent trading in 1986, by removing the *locus standi* of creditors: See, for example, the written statement of Mr Alexander Fletcher MP at: HC Deb 05 June 1985, vol 80, col 178W where this is alluded to, also; Hicks, 'Wrongful trading – has it been a failure?' (n 605) 136. It does not appear that, in the consultation relating to assignment, that this factor was considered at all. Undue pressure being placed on directors is also a core concern in the area of disqualification, as discussed at: 2.47.

with D&O insurance would be prime targets for this sort of tactic, which may lead to an increase in premiums across the board. Whilst the public at large would no doubt be relatively unsympathetic to such individuals – perhaps suggesting that there is 'no smoke without fire' – there is a strong possibility that even honest and competent directors could be targeted. If true, this could have a wider negative impact on the economy as it may disincentivise individuals from taking up directorships within companies for fear of litigation should things go wrong. This would therefore upset the balance between access to limited liability and appropriate levels of regulation. As explained in Chapter 1, it has to be accepted that in a market based economy businesses will fail. However, in instances where there has been no impropriety this should not necessarily condemn a person to financial ruin on the back of ambulance chasing. One consultee specifically mentioned the chilling effect that this may have on the taking up of directorships by insolvency experts, such as Chief Restructuring Officers. These individuals often come in to companies as change agents to turn around a business which may otherwise be destined for insolvency. Any such impact would clearly be out of step with the UK's rescue culture and wider enterprise policy.

Collectivism

5.20 As a minor point of policy surrounding IA 1986 litigation powers, it should be noted that they are drafted in the full spirit of distributions being made *pari passu*. A core objective of the private enforcement provisions is to ensure increased returns for all unsecured creditors. It appears to this author that there may be policy issues with having one creditor buy out the claim, to eventually secure a benefit above and beyond that of her fellow creditors. Clearly there is an inherent risk in her doing so, and that risk may become her reward. But, looking at this issue through the spectacles of collectivism, it appears to contort the original ethos of the provision. In line with the author's approach this would therefore be undesirable in terms of the effectiveness of the mechanisms, given their objective as being to compensate an entire body of creditors. Yet, if it were to be a condition of assignment that proceeds were to be shared (equally) there would be no incentive for a creditor, or indeed any other person, to buy the claim.

ASSIGNMENT IN PRACTICE

5.21 At this juncture, it is worthwhile exploring briefly how assignment might operate in practice. In doing so the author investigated the types of products and services that specialist claims companies might offer to officeholders wishing to sell IA 1986 actions. These companies will without doubt be the primary purchasers of such claims. It would certainly, for the purposes of the author's research, have been informative to gain the perspective of officeholders so as to determine how *they* will approach the question of assignment in practice. However, in terms of the scope and methodology of this thesis, accessing the information provided by claims companies has been the more straightforward option. It is likely also the most useful, as these companies will invariably offer assignment agreements on standard terms, which are therefore likely to be representative of the majority of assignments that will take place. Information was readily available from Manolete Partners plc ('Manolete'), which is the largest insolvency litigation funder in the UK.[634] A survey of IPs conducted by R3 suggests that

[634] This is Manolete's own claim. See Manolete Partners Plc, 'R3 Survey shows the majority of IPs who use litigation funding use Manolete Partners' available at <http://bit.ly/2cjHqPg> accessed 01 August 2016.

in circumstances where an officeholder chooses to make use of a litigation funder, the majority choose Manolete.[635] It offers officeholders two assignment options:[636]

> (a) a Sale and Purchase Agreement: a sale of 100 per cent of the interest in the case for a lump sum cash payment to the insolvent company; or
>
> (b) a Funding Agreement: a smaller initial payment is made to the insolvent company, but with its retention of an ongoing economic interest in any proceedings taken. The retained interest is a minimum of 50 per cent though, depending on the quantum of any eventual recovery, this ratchets up to a maximum 75 per cent (in the insolvent company's favour).

Option (a) presents a straight forward sale agreement. The officeholder will be presented with a fixed-sum offer, which she can either take or leave. As described by Manolete themselves, the primary benefit of this option is quick turnaround for creditors: '[y]our file can then be closed. Final costs invoiced and distributions made'.[637] However, option (b), what Manolete calls its 'traditional purchase' offer, may prove to be the more favoured amongst officeholders. Any 'cut and run' offer of a fixed lump sum, as per option (a), is likely to result in a proportionately small return for creditors, or at least one smaller than could potentially be obtained under option (b). Officeholders may therefore face pressure from creditors to 'gamble' on the higher-risk higher-reward option. In either circumstance, even where an economic interest is retained by the insolvent company in proceedings, Manolete undertakes to indemnify the officeholder from any adverse costs, and covers its own legal costs. As a result, no ATE insurance is required and the entire process is carried out at virtually no risk to the officeholder or the insolvent company. Because of this, following the implementation of the LASPOA 2012, and as its effects in insolvency litigation take hold, it seems inevitable that a

---

635 Walton, 'Insolvency Litigation and the Jackson Reforms – An Update', 2.3.
636 Manolete Partners Plc, 'Newsletter Autumn 2015' available at <http://bit.ly/2bIyOpp> accessed 01 August 2016.
637 ibid.

greater percentage of officeholders will consider making the switch from the combined CFA/ATE approach to one of assignment; especially in small cases, where costs saving is essential. The Government has commented that the CFA is unlikely to be affected by the introduction of assignment.[638] When taken in isolation this may be true, however, when joined with the potential effect of the LASPOA 2012 reforms this seems unlikely to the present author. In fact, it is argued here that assignment may simply go on to replace the CFA as the go-to method of dealing with IA 1986 litigation for the future.

5.22 It should also be noted that the assignment of IA 1986 actions was permissible in Scotland before the introduction of the SBEEA 2015.[639] Therefore, it is by no means an unprecedented step. More importantly, however, it provides a valuable point of observation in understanding how it may be utilised in the English and Welsh context. In its response to the *Transparency & Trust* consultation, the Institute of Chartered Accountants of Scotland stated that, given the substantive legal difficulties, the experiences of their members suggest that assignation is relatively rare.[640]

CONCLUSION

5.23 This chapter first began by assessing the problem that the new power of assignment purports to overcome – funding. It has been argued however that funding may no longer be as significant a hurdle as it once was. The author has suggested that the focus ought to, instead, turn to an investigation of the substantive legal and practical difficulties faced by IPs. There may not be a simple solution to those problems; a point that will be revisited in the next chapter of this thesis where the author considers more

[638] Assignment Impact Assessment, para. 12.
[639] In Scotland, however, the process is known as 'assignation'.
[640] T&T Consultation Responses.

fundamental reforms to access to limited liability itself. There is also a further dimension to consider in that, even where an assignee is successful, there is no guarantee that the defendant will be able to pay due to her impecuniosity. Whilst assignment clearly does not aim to target these difficulties, they must be considered as a factor in determining the potential that it has for the increasing the number of actions brought which – it must be remembered – was the objective of the provision as set out in the Paper. If the author is correct in his assertion that funding claims is an issue on the periphery, then one possible inference to be drawn from that is cases will not be assigned very often. Another possibility, as is cautiously suggested here, is that assignment, whilst not necessarily increasing the number of cases or returns for creditors, may in fact become the 'go to' device for officeholders when dealing with IA 1986 claims instead of the CFA. This is because it overcomes some of the uncertainties and disadvantages of a combined CFA/ATE approach post-Jackson Reforms. But, it should not be held out by the state as a magic bullet to all the problems of commencing IA 1986 actions. In fact, this chapter has also identified many of the dangers with assignment itself. Put simply, assignment on its own is insufficient to improve the effectiveness of the wrongful and fraudulent trading provisions by increasing the number of claims brought. As such, the author is confident that they will retain their status as 'paper tigers' following the SBEEA 2015.[641] The trade-off for this only-marginally-improved position, however, is to create a very real potential for negative consequences upon the enforcement regime as a whole; brought on, in the main, by a

[641] This is in reference to both Andrew Hicks and Carol Cook who have previously stated that the wrongful trading remedy may be seen by directors as nothing more than a 'paper tiger': see Carol Cook, 'Wrongful trading – is it a real threat to directors or a paper tiger?' (1999) 3(Apr) Insolv L 99; Hicks, 'Wrongful trading – has it been a failure?' (n 605).

surge in nuisance claims. Thus, for directors this is no doubt a worrying development. For IPs practically speaking, it offers an interesting escape from the previous complexities and uncertainties of a combined CFA/ATE approach, though will likely have a limited impact upon their decision as to whether a director is pursued or not – as appears to be the Scottish experience. For the creditor, the author does not anticipate that there will be any noticeable increase in returns, though there will no doubt be the occasional success. And, there is also no doubt that it is these successes that will be latched on to by the state in any future evaluations.

Part IV

REFORM AND FINAL CONCLUSIONS

6

REFORMING LIMITED LIABILITY

6.1 Governmental attitudes towards limited liability have already been set out in the first chapter of this thesis.[642] By way of adumbration it may be reduced to the following: limited liability is viewed as necessary in stimulating and facilitating a capitalist economy. Incorporation in the UK is amongst the simplest and cheapest in the whole of Europe. Policy makers understand, indeed embrace, the inevitable abuse that follows from such unfettered access to limited liability. The private enforcement mechanisms explored throughout this thesis exist to provide a means of redress to creditors and regulate undesirable conduct. The primary public mechanism of dealing with undesirable conduct, disqualification, is inextricably tied to and, in some ways, an inevitable consequence of unrestricted access to limited liability. It exists as a means of reassuring creditors that, in what is a fertile landscape of moral hazards harbouring considerable scope for excessive risk taking, misconduct will not go unchecked. In other words, both public and private enforcement regimes provide a trade-off necessary to legitimise, in the eyes of creditors and the wider public, such open access to the *corpora ficta*.

[642] 1.2

THE CASE FOR REFORMING LIMITED LIABILITY

6.2 As has been addressed in some detail in the preceding chapters, each of these mechanisms has its shortcomings. In some cases this is a gross understatement. What is apparent however is that each share a fundamental detail in common with the other which, it is suggested, creates an insoluble barrier to increasing effectiveness: each mechanism operates *ex post facto*. These mechanisms are solely concerned with damage limitation. They are a form of reactionary, not preventative, medicine. It follows that, despite the shortcomings of any individual mechanism, the underlying problem, namely permitting free access to limited liability in the first place, remains. Save for individuals with a track record of misconduct who can readily be identified (and disqualified), there is no accurate means of an *ab initio* 'filtering out' of those who will later be revealed as undesirable managers. It follows still that simply tinkering with, or even repealing and replacing existing mechanisms entirely, is unlikely to stopper the problem. As such, it is argued here that *ex post facto* mechanisms are unavoidably condemned to at least partial failure because they do not address this underlying cause. The reader will by now understand where the present argument is going: access to limited liability itself ought to be curtailed *ex ante*. This is not as radical as it first sounds, and it is by no means a new argument. Indeed, the idea is noticeably still very much alive amongst business and professional communities, as evidenced in the response to the recent *Transparency and Trust* consultation exercise;[643] a matter dealt with in due course. However, free access to limited liability is a cornerstone emblem that permeates the very fabric of capitalist society. Any interference with it has therefore been routinely

[643] See the T&T Discussion Paper (n 14) and the T&T Government Response (n 223). See also the T&T Consultation Responses (n 612).

rejected by governments of all colours.[644] Yet, as will be shown, the benefit that limited liability supposedly brings can be disputed in many cases, particularly in owner-managed companies. It is suggested here that limited liability ought not be seen as some sacred cow never befitting of reform. It is entirely counter-productive for any government to bury their heads in the sand as to the source of the problem for fear of upsetting the *status quo*, but then undertake merely to implement remedial, less effective, measures after the fact. Even worse, is to hold out (politically or otherwise) those remedial measures as evidence of taking a 'tough stance' on director misconduct, when the actuality is a stark lack of resolve in being willing to address the underlying cause.[645]

6.3 More should be said as to the benefits of limited liability. In their seminal work on the economics of corporate law Easterbrook and Fischel stated the most touted benefits to be as follows:[646]

(a) Limited liability decreases the need to monitor agents by promoting diversification of investment.

(b) Limited liability reduces the costs of monitoring other shareholders; this is because individual shareholder wealth is rendered irrelevant.

---

[644] As is evident most recently in the *Transparency and Trust* consultation from the rejection of educating directors as a pre-cursor to permitting accessing limited liability. As will be discussed later in this chapter, this is in spite of a considerable proportion of consultees being in favour of such an idea. See 6.20.

[645] There has been a great deal of political posturing on the issue over the years. This was especially evident during the passage of the SBEEA 2015. See for example Rowena Mason, 'Vince Cable To Bring In Tougher Penalties For 'Dodgy Directors' *The Guardian* (19 April 2014) <http://bit.ly/2q6crfL> accessed 17 May 2016; 'Vince Cable proposes tougher rules for directors' *BBC News* (15 July 2013) <http://bbc.in/2rGgX51> accessed 17 May 2016.

[646] The following list of advantages of limited liability is paraphrased from Frank H Easterbrook and Daniel R Fischel, *The Economic Structure of Corporate Law* (Harvard University Press 1991) 41-44.

(c) The free transfer of shares permits shareholders to sell easily, which provides managers with an incentive to operate the corporation efficiently to prevent being replaced.

(d) Limited liability allows shares to be fungible, and their valuation is determined by the income stream generated by the corporation's assets. Rather than being based upon investors' wealth, individual wealth of other shareholders is in fact irrelevant. A lack of fungibility would, according to Easterbrook and Fischel, impede the acquisition of shares.

(e) Limited liability permits market prices of shares to reflect additional information about the value of a firm's prospects as all shares are traded on the same terms.

(f) Limited liability permits more efficient diversification. Risk is reduced by diversifying, which in turn permits the raising of capital for corporations at a lower cost. In a system of unlimited liability diversification *increases* risk as one single business failure could lead the shareholder to become bankrupt.

(g) Managers, in knowing that investors hold diversified portfolios, can take bold business decisions without exposing them to bankruptcy. In unlimited liability situations managers would reject projects deemed too high-risk.

When considering closely held corporations however, as has been the author's primary focus throughout this thesis, many of these benefits are merely theoretical.[647] In fact, Easterbrook and Fischel concede that the limited separation between management and risk bearing found in close corporations has 'profound implications'[648] for limited liability. Indeed, limited liability cannot be said to reduce the costs of monitoring in owner-managed companies as the investors are also the decision makers. Owner-managers generally do not have large diversified investment portfolios. The opposite is more likely to be true; a large proportion of an individual's assets will be ploughed in to the single company. As such, owner-managers make for inefficient risk bearers.[649] Easterbrook and Fischel however suggest that this lack of diversification induces

[647] See also Freedman and Godwin (n 281) 233.
[648] Easterbrook and Fischel (n 5) 55.
[649] This is dealt with in some detail in Easterbrook and Fischel ibid ch 9.

owner-managers to have more care when taking business decisions.[650] It is submitted however that this is not necessarily the UK position, when one considers the data explored previously.[651] The fungibility of shares is practically irrelevant in the closely held corporation, as the object is generally to restrict transfer by the utilisation of pre-emption agreements or similar clauses within the articles. Furthermore, and crucially, owner-managers are often (but not always[652]) forced to contract out of limited liability should they seek capital from adjusting creditors[653] such as banks. In short, as was concluded by Freedman and Godwin in their empirical analysis of the micro-business, often for small companies the burden outweighs the benefit.[654]

6.4 The result of this analysis therefore prompts the question: 'why the limited liability company?'. It is this author's belief that in many cases the choice of the limited liability company is one prompted by 'marketing' efforts, for example of formation agents and accountants, which deify the limited liability company – citing an untold wonder of tax advantages and 'risk-free' trading – rather than necessarily any process of careful decision making on the part of the incorporator as to what is most appropriate for his business needs.[655] It is argued here that the owner-manager demographic presents

---

[650] ibid 237.

[651] See 2.15 Even if their contention is true, however, there is still a visible problem for which the availability of enforcement mechanisms is clearly seen as being desirable.

[652] In Freedman and Godwin's study (albeit of a small sample), 53.6 per cent (67 respondents) of directors and/or their spouses had provided personal guarantees. In the vast majority of cases these were to banks: Freedman and Godwin (n 281) 246. Moreover, Hicks in his survey found 75 per cent had given personal guarantees: Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (n 18) 9.

[653] An adjusting creditor is one that can alter the terms on which it provides credit, for example, a bank. In doing so, the adjusting creditor can consider risk, based on a variety of factors, in determining whether to extend credit, rates of interest, or other terms.

[654] Freedman and Godwin (n 281) 233.

[655] In the words of Freedman and Godwin, owner-managers are 'victims of a culture which encourages incorporation indiscriminately': Freedman and Godwin ibid 233; Anecdotally, one *Transparency & Trust* consultee (an insolvency practitioner) complained that he was often told

itself as one where limited liability could be curtailed or removed, quite simply because the benefits are mythical.

6.5 Of course, the economic sense of doing so must be considered. If the wealth benefits derived from free access to limited liability for owner-managers exceeds the cost[656] of misconduct then it should be accepted as a necessary evil. If the reverse is true however, then reform ought to be pursued to address the imbalance. The very existence of private enforcement mechanisms suggests that there *is* a perceivable imbalance between the two economic factors. If there was no such imbalance, then it is suggested there would be no appetite to permit recourse for creditors and others through regulation.[657] Furthermore, it is suggested the existence of a public enforcement regime, namely disqualification, creates the impression of an even starker imbalance. It indicates that private enforcement is simply not enough on its own; state interference to the extent of *banning* individuals from directorial office is deemed as necessary. Given that disqualification specifically is utilised most frequently against owner-managers, this suggests that the imbalance must be wider in respect of this demographic. This latter point is also borne out by Easterbrook and Fischel, who suggest that the likelihood of managers engaging in risky behaviour is far greater in close corporations.[658]

owner-managers had incorporated for 'tax' reasons; but yet were completely ignorant as to directors' duties; See also the discussion had earlier in this thesis: 1.6.

[656] Cost here is meant in the broadest sense, i.e. not just in monetary terms but as regards any wider societal impact.

[657] This is because the cost of introducing and maintaining enforcement mechanisms would by definition be undesirable. The attitude would instead simply for the loss to lay where it fell (i.e. at the feet of unsecured creditors).

[658] Easterbrook and Fischel (n 5) 56. Interestingly, this conflicts somewhat with the point made by those authors previously in that owner-managers are likely to be more risk averse in their decision-making as a result of the closely held shares – a point also raised in Rizwaan Mokal, 'An Agency Cost Analysis of the Wrongful Trading Provisions: Redistribution, Perverse Incentives and the Creditors' Bargain' (2000) 59(2) CLJ 335, 353.

Moreover, it is compounded by the greatly reduced advantages of limited liability in close companies, addressed previously. The very *existence* of enforcement mechanisms provides fertile ground for argument that access to limited liability ought to be curtailed. If the mechanisms proved effective, then the current policy could be tolerated. If shown to be largely ineffective however, as is suggested,[659] then methods to limit access to limited liability should be explored.

6.6 A question therefore arises as to what specifically could be done to redress the balance. If those with a temerarious attitude towards risk can be prevented from accessing limited liability in the first place the issues created by free access are mitigated against and, further, the need for *ex post* regulation is reduced (thereby saving further cost). By way of analogy, an envisaged optimal form of limited liability might be compared to a flood barrier. The barrier regulates the tidal waves that are company directors. The barrier prevents the worst tidal waves from breaching its defences. Such control inevitably causes an inconvenience for passing river traffic. But, society bears the inconvenience, and the cost of maintaining the barrier, to avoid certain disaster. At present however, in the context of limited liability, the barrier is perpetually lowered and therefore all ills pass through with considerable ease, without challenge, and entirely unmitigated against. Instead, the approach is simply to rebuild after the fact, at an increased long-term cost over prevention. To raise a barrier against entry would be to deal with the problem at source. Some delinquents may still permeate the defences, but the prospect of that occurrence is minimised; the worst offenders are stopped in their tracks, or their capability for destruction is diminished. The remainder of this

[659] This is largely the substance of the author's thesis, in fact.

chapter, then, will go on to consider several options open to policy makers in order to curtail the negative effects of limited liability at source. It is submitted that effective measures should go some way towards restoring the equilibrium between the cost of misconduct and any derived wealth benefits. This will be approached on two fronts, largely (but not exclusively) with a focus on owner-managers. The reason for this focus is as a consequence of the large proportion of enforcement action being taken against that demographic. Moreover, there is simply more data available for analysis in respect of owner-managers. It is therefore clearly ripe for close scrutiny and an ideal target for reform. The author will approach this issue firstly by identifying some of the more traditionally suggested reform methods that focus on a burden placed upon the *company* for it to be lawfully incorporated (i.e. as affecting the 'owner'). The chapter will deal with abolishing limited liability for owner-managers and minimum share capital requirements. Secondly, by dealing with the less well researched area of what can be done as against *individual's* themselves (i.e. as affecting the 'manager'). This will address minimum age requirements for company directors and minimum educational requirements.

ABOLISHING LIMITED LIABILITY FOR OWNER-MANAGERS

6.7 It has been set out earlier in this thesis that a considerable proportion of those directors who are disqualified are so called owner-managers.[660] It has also been stated that many of the benefits attributed to limited liability are absent in the case of the closely held corporation. Incidentally, it is therefore this demographic least likely to be affected by mechanisms such as disqualification. Simply put, they don't have very far

[660] 2.15.

to fall and can resume trading, albeit in an unlimited form, with little difficulty.[661] The somewhat radical solution therefore would be to abolish limited liability for the small owner-managed corporation. In doing so, a considerable part of the problem that public and private enforcement mechanisms alike deal with is removed. The empirical findings of various commentators suggest that a regime of *unlimited* liability is generally the most efficient for owner-managed companies.[662] As such, society would continue to derive benefits from similar levels of entrepreneurial activity but in a way that reduces the wanton transfer of risk to creditors; reduces costs for owner-managers; and all but eliminates moral hazards. The need for and utilisation of disqualification as an enforcement mechanism would in essence disappear for this class of persons, as the cost of risk taking is born by the individual concerned. Given the number of disqualifications levied at owner-managers, overall utilisation would be greatly reduced. For creditors, bespoke enforcement mechanisms would be unnecessary, as the general law provides sufficient means of recourse already. Naturally, it is conceded that this is only a partial solution as it does not deal with wider misconduct arising from access to limited liability in non-owner-managed companies.

6.8 One less radical alternative to abolition is the creation of a new corporate entity specifically designed to be used by the owner-manager. It would adopt the structural and tax benefits of a limited liability company, but trade on an unlimited basis. Commensurate benefits, such as reduced transparency of corporate affairs would also attach. Whilst this seems to present an interesting 'third way' it is argued here that it merely perpetuates the problem. As Freedman and Godwin explain, the idea of a revised

[661] 2.15.
[662] Freedman and Godwin (n 281) 266; Halpern, Trebilcock and Turnbull (n 22).

corporate form is frequently pursued by commentators[663] due to their 'misunderstandings surrounding the reasons for incorporation'[664] and the supposed benefits. These misunderstandings have led to an undue focus 'on incorporated firms to the exclusion of unincorporated firms'.[665] In this author's words, the cultural deification of incorporated status has led policymakers to blindly bend over backwards to reform the incorporated form, as opposed to recognising that in some instances it simply does not provide benefit. As such, policymakers and commentators must start to seriously consider abolition in respect of the owner-manager and begin to encourage unincorporated forms of doing business.

6.9 Moreover, such an entity already exists, namely the 'private unlimited liability company'. These companies are exempt from filing annual returns or accounts, and do not need to utilise the 'Limited' prefix. [666] If a specialised form for owner-managed companies is preferred, adoption would have to be mandatory to have any meaningful impact. One other issue with this approach is that access to the full-blown limited liability company would have to be based on a criterion of how closely held shares in a corporation are. No doubt attempts would be made by lawyers to circumvent the requirements to achieve limited liability status, if it was deemed to be desirable.[667] In principle, then, the author is of the view that in any approach unlimited liability must

---

[663] For example, Michael Chesterman, *Small Businesses* (Sweet & Maxwell, 1972); John Farrar, Nigel Furey, and Brenda Hannigan, *Farrar's Company Law* (3rd edn, Butterworths 1998).
[664] Freedman and Godwin (n 281) 233.
[665] ibid.
[666] They are hugely underused however, for obvious reasons: the latest statistics suggest that the total number of unlimited companies in existence accounts for 0.1 per cent of total companies on the register. See: CH, *Companies Register Activities 2015-2016* (2016) <http://bit.ly/2pTlhBq> accessed 14 April 2017, Table G1.
[667] In true *Salomon v A Salomon & Co Ltd* [1896] UKHL 1 style; a case that needs no explanation here.

be the common denominator. This factor would remove a considerable portion of present difficulties, and substantially reduce reliance on *ex post* enforcement mechanisms, in one fell swoop. This can only be a good thing. Entrepreneurs would fall back on the unlimited liability company, or preferably unincorporated forms, and as such the economic aspects should remain largely unaffected. To be successful, however, a considerable cultural shift in attitudes toward the limited liability company would be required, as explored previously. There is much that policymakers can do to help in this regard.

MINIMUM SHARE CAPITAL REQUIREMENTS

6.10 Another solution is the introduction of minimum share capital requirements for private companies.[668] In short this is desirable because undercapitalisation promotes excessive risk-taking.[669] Over the years the idea has been periodically revisited,[670] though Anglo-American corporate law has traditionally rejected it as an inhibition on entrepreneurial freedoms. Its implementation would provide something of a safety net for creditors. It would ensure that shareholders pay an identifiable and irreducible price for their limited liability status and the benefits attached to it. The higher the minimum

[668] It has been shown, previously, that most private limited companies adopt very low share capitals indeed: 3.45.
[669] Easterbrook and Fischel (n 5) 59.
[670] The Jenkins Committee considered the matter, though ultimately ruled it out as being to straightforward to avoid, at DTI, *Report of the Company Law Committee* (Cmnd 1749, 1962) para 27 (The Jenkins Report). The issue was considered in passing by the Cork Committee when introducing the idea of wrongful trading. The Committee suggested that it (wrongful trading) would 'go a long way to meet the criticisms of those who complain of the absence of a minimum paid-up share capital' at The Cork Report (n 68) para 1785. The Committee also clearly expressed distaste for under-capitalisation (para 1815) and stated that those trading when heavily undercapitalised would often be trading wrongfully (para 1785). The later 1973 DTI Whitepaper again commented on the matter; committing to the idea in terms of public corporations, though less certain about imposing similar requirements on private enterprise. See DTI, *Company Law Reform* (Whitepaper, Cmnd 5391, 1973) para 33 (1973 Whitepaper).

capital threshold, the more that shareholders risk. The lower it is, the less there is to lose. As with the *ex post* mechanisms discussed throughout this thesis, the aim of minimum capital requirements is the protection of creditors. It prevents access to limited liability – full stop – for those unable or unwilling to put their money where their mouths are. One other cited advantage has been as a 'deterrent to frivolous incorporations'.[671] For this reason, it has been referred to as being an 'entrance fee'.[672] Presently, in English law, there are no minimum capital requirements for private companies.[673] Out of the sample of disqualified directors analysed earlier in this thesis, 80.0 per cent of companies connected to those disqualifications had a share capital of no more than £100. 91.8 per cent of companies within the sample held a share capital of no more than £1000.[674] Indeed, it should come as no surprise to the reader that the vast majority of English companies incorporate with a share capital of less than £100.[675] The reason for doing so could not be put more exquisitely than it has been by Messrs. Gilbert and Sullivan, whose words still, in the present day, have an eerie significance:

---

[671] 1973 Whitepaper (n 670) para 33.

[672] Prentice, 'Corporate Personality, Limited Liability and the Protection of Creditors' (n 26) 102.

[673] Banks are a known exception to this general rule. For detail see: Garvey and Others (n 21) div A, ch 5. Public companies of course must have a minimum capital of £50,000 by virtue of the CA 2006, s 763.

[674] 3.45.

[675] Many, in fact, do so for £1 or even a single penny. In previous years, CH have provided a breakdown of the number of corporations by share capital though it appears this has ceased since 2013. The last available information, taken from the register as at 31 March 2013, suggests that in England and Wales 2,188,800 companies had a share capital of up to £100. This represented 84.6 per cent of the total companies on the register. See: CH, *Statistical Tables on Companies Registration Activities 2012-2013* (n 290).

Director Liability in Insolvent Companies

Some seven men[676] *form an Association,*
(If possible, all Peers and Baronets)
They start off with a public declaration
To what extent they mean to pay their debts.

That's called their Capital: if they are wary
They will not quote it at a sum immense.
The figure's immaterial - it may vary
From eighteen million down to eighteen pence.

I should put it rather low;
The good sense of doing so
Will be evident to any debtor.
When it's left to you to say
What amount you mean to pay,
Why, the lower you can put it at, the better.[677]

Practicalities

6.11 As Armour notes, a minimum capital requirement taken alone would be largely ineffective without complementary anti-avoidance provisions in place to ensure that the capital has actually been contributed,[678] and is maintained.[679] Of course, if the stated effect is to reduce creditor anxiety it must be a minimum *paid-up* share capital requirement. Otherwise, it would be one having no teeth, to be avoided with considerable ease. This was the very fear expounded by the Jenkins Committee in considering it as a possible solution, leading them to dispense with the idea with relatively short shrift.[680] Even should anti-avoidance mechanisms be introduced

[676] Of course this is a reference to the original minimum number of stockholders required to form a company.
[677] William S Gilbert and Albert Sullivan, 'Mr Goldbury' from the opera *Utopia Limited* (1893). The full libretto is available at <http://bit.ly/2q15iNm> accessed 15 May 2017.
[678] John Armour, 'Legal Capital: An Outdated Concept?'(2006) 7(1) EBOR 5, 10.
[679] Issues surrounding capital maintenance, for example, by utilising risk-free investments is considered at Easterbrook and Fischel (n 5) 60. Furthermore, Cheffins comments that simply enshrining a level of capital in the company's articles does not guarantee that it will be available when called upon: Brian Cheffins, *Company Law: Theory Structure and Operation* (Clarendon Press 1997) 531.
[680] The Jenkins Report (n 670) para 27.

however, the increase in additional monitoring costs to ensure compliance would no doubt be considerable.

6.12 That aside, one of the main barriers is determining how the 'minimum' ought to be calculated.[681] There are dangers in setting the figure too high, as this would upset the balance between protecting creditors and encouraging entrepreneurship.[682] Inevitably, it would be the small man that would suffer as a result. However, set too low and the net effect is that creditors remain vulnerable (though perhaps less so) and the increased costs of monitoring are likely to outweigh any perceivable benefits. It is also far too simplistic, as is done with the public company, to adopt a one-fits-all approach. Any 'minimum' would have to be variable so as to account for the type of trading activity envisaged, and therefore the risks commensurate with it. Accurately calculating what the threshold ought to be for any given entity is an ineradicable difficulty. Presumably the solution would take the shape of a complex statutory algorithm. Aside from the obvious administrative costs in development, this seems to be an untidy solution and one probably resigned to failure unless it was 'just right'. It is the traditional *Goldilocks* dilemma. It is not even clear whether it would be possible to fashion such a thing with any level of accuracy in the first place.

---

[681] This is an issue recognised by many of the commentators. For example, see: Easterbrook and Fischel (n 5) 60; Armour (n 678) 11. The DTI Whitepaper in 1973 did suggest a £1000 minimum capital threshold (fixed); though it appears this figure was plucked out of the air for illustration purposes and not intended to be treated as a serious suggestion. See 1973 Whitepaper (n 670) para 33.

[682] Armour suggests that an inability to gain access to limited liability may deter entrepreneurial activity, and cites a study showing a negative correlation between the size of minimum capital requirements and self-employment during the 1990's at Armour ibid 18. For details of the study cited see John Armour and Douglas J Cumming, 'Bankruptcy Law and Entrepreneurship', University of Cambridge ESRC Centre for Business Research (Working Paper No 300 March 2006).

6.13 A crucial factor to consider is that the introduction of a minimum capital requirement does not necessarily protect creditors. This is evident in the case of the non-adjusting creditor. One of the problems most observable from the statistics explored previously in this thesis is that most disqualifications arise from the non-payment of Crown debts, in undercapitalised companies, that are largely owner-managed.[683] However, Armour has argued that a minimum capital requirement would have no effect upon the Crown in its capacity as a tax creditor given it extends credit on an involuntary and *ipso facto* non-adjusting basis.[684] This is because tax liabilities do not arise until the company itself is operating and carrying out transactions that are taxable.[685] Furthermore, other involuntary creditors such as tort victims are faced with the same difficulties set out previously, namely that determining an adequate level of capitalisation is an inherently difficult task. A minimum capitalisation requirement, it is submitted, is only as useful as the accuracy of the method of determining what the minimum is. A tort creditor may find that the company is *undercapitalised* despite strictly enforced minimum capitalisation legislation. The extent of any benefits brought about by minimum capitalisation are therefore not, it is suggested, as attractive as at first blush.[686] One final issue taken by Armour on this point relates to the position of trade creditors as being *de facto* non-adjusting in many cases.[687] While this seems counter-intuitive, it must be correct that trade creditors will be conscious of ensuring

---

[683] 3.45-3.47.
[684] Armour (n 678) 20.
[685] ibid.
[686] On tort creditors and their interface with limited liability generally, see: David W Leebron, 'Limited Liability, Tort Victims and Creditors' (1991) Colum LRev 1565.
[687] Armour (n 678) 20.

that transaction costs incurred are 'relative to the amount at stake'.[688] Indeed, it would seem odd to suggest that a commercial wholesaler of wheat, for example, would offer more (or less) favourable terms of credit to one party over another on the basis of their capitalisation. The scope and cost of the inquiry is likely beyond the scrutiny of all but the most fastidious of creditors.[689] As such, Armour concludes rather pithily that it is in fact 'hard to find a category of non-adjusting creditors for whom minimum capital rules offer useful protection'.[690]

The Death of Minimum Capitalisation

6.14 It therefore does not require much by way of analysis to conclude that, whilst a minimum share capital would likely have a significant impact in terms of deterring risky corporate activities and 'casual incorporation', it is a concept plagued with difficulties. Not only is it something of an impracticable and haphazard solution to the problem at hand, it also serves to threaten rates of entrepreneurial activity; arguably with limited benefit in return. The protection supposedly offered to creditors (which is, after all, the primary concern here) ought not be overstated. Whilst, originally, minimum capital requirements were the mainstay across much of continental Europe, following the seminal decision in *Centros*[691] much of this has since been abandoned or reformed.[692]

---

[688] ibid. Armour cites empirical evidence of this claim from a study conducted by Chee K Ng, Janet K Smith and Richard L Smith, 'Evidence on the Determinants of Trade Credit Terms in Interfirm Trade' (1999) 54 J Fin 1109.
[689] A point also raised by Williams and McGee (n 454) 26-27.
[690] Armour (n 678) 21.
[691] ECJ Case 212/97 *Centros Ltd v. Erhvervs-og Selskabsstyrelsen* [1999] 2 CMLR 551.
[692] For two interesting comparative studies on the issue see: Wenjing Chen, 'Abolition of legal capital requirements under Chinese Company Law 2014 and its potential influence: a comparative study in selected countries' (2014) 35(12) Co Law 371; Khodr M Fakih, 'The one-member company: a comparison study of the one-member company in France, Europe, United States and Lebanon' (2014) 25(6) ICCLR 221.

China, as recent as 2014, abolished its own minimum share capital requirements.[693] Although some have called for the matter to be revisited in the UK context,[694] it would seem the death knell is tolling for minimum capital rules across the globe – and, it is submitted, for good reason.

MINIMUM AGE REQUIREMENTS

6.15 Current law already imposes minimum age requirements for company directors. Section 157 of the Companies Act 2006 puts that age at 16.[695] The argument to examine here then is whether it is worthwhile revisiting the minimum age and raising it in the hope of deterring and preventing further misconduct. It is worth noting before the 2006 Act there were no age barriers whatsoever to directorship and so this was something of a step change. The same Act removed the maximum age for directors, previously fixed at 70, and provided that at least one director must be a natural person.[696] The idea behind this suite of changes was to permit better enforcement of corporate legal obligations, therefore improving compliance, by ensuring at least one natural 'adult' director was available to proceed against.[697] Milman has argued that the reason for not selecting 18 as an appropriate age is 'hard to justify'.[698] Indeed, it is something of an oddity of

---

[693] Chen (n 692).

[694] For example, Philip King chief executive of the Institute of Credit Management has stated he would 'absolutely' be in favour of a minimal share capital for small companies: Sarah Houghton, 'Interview with Philip King' Recovery (R3, Spring 2012) 46. Moreover, whilst Milman accepts that minimum capital requirements offer little protection to creditors, he suggests the issue ought to be revisited: Milman, *Governance of Distressed Firms* (n 10) para 6.5. Also, see the much earlier David Milman, 'The 'phoenix syndrome'' (2001) 6 Insolv L 199.

[695] The SS also has the power to make regulations to exempt individuals from the age requirements. To date no such regulations have been made. See CA 2006, s 158.

[696] Pursuant to the SBEEA 2015, s 87, this position is to change once more. The section introduces to the CA 2006 ss 156A-C. Although not yet in force, upon implementation, corporate directors will be banned entirely (CA 2006, s 156A), with exceptions (CA 2006, s 156B). All existing corporate directors will cease holding their office on an appointed day (CA 2006, s 15C).

[697] DTI, *Company Law Reform* (Cm 6456, 2005) 276 (2005 Whitepaper).

[698] Milman, *Governance of Distressed Firms* (n 10) 9.

English law[699] that a person may command the responsibilities of a director at 16 but that same individual, in her personal capacity, will usually be unable to enter most types of contract.[700] No doubt the reason for imposing what is arguably quite a low age requirement (as is invariably the reason put forward for these things) was so as not to deter entrepreneurship.

6.16 On the one hand, then, it is hard to disagree with the sentiments of those such as Milman. It is suggested that if the age is to be increased there is little credibility in any argument that it should be *greater* than 18, that being the age of majority. On the other hand, imposing minimum age requirements beyond what is legally necessary to enforce compliance with companies' legislation, could be perceived as unduly restrictive. Is it that society simply does not trust 16 and 17 year olds with such responsibilities, or does it relate to lack of experience or education, or perhaps other factors?[701] Regardless, in the context of director liability, the correct approach here must be to assess whether those in the under 18's demographic can be identified as being 'problem directors'. If so, other matters aside, some benefit may be derived from increasing the minimum age.

6.17 It was reported in 2005, before the imposition of the age requirement, that there were approximately 500 companies with a director younger than 16.[702] No figures were given as to the proportion of directors who were 16 or 17. In any case, it seems likely

[699] For example, in Australia the position differs (and is arguably more sensible) in that it imposes minimum age requirements of 18: Corporations Act 2001, s 201B(1).
[700] For fear of them being unenforceable as against a minor. For more detail see Hugh G Beale (ed), *Chitty on Contracts: Volume 1* (32nd edn, Thomson Reuters 2015) ch 9.
[701] The author makes the point that everyone must start somewhere. Moreover, training in general is deficient across the board as will be explored below. It is simply not the case that upon turning 18 a person is suddenly all the more well-equipped to deal with directorial responsibilities. The focus of policymakers, as appears to be the case, must focus instead on the age necessary to be able to enforce legal obligations against directors on a personal liability basis.
[702] 2005 Whitepaper (n 697) 276.

that we are dealing with very small numbers. This author's own analysis of the DDR reveals that there were zero disqualified directors on the register below the age of 18 as of November 2013. Discounting records where individual dates of birth were not recorded, leaving a total of 7,178 for analysis, it was determined that the youngest disqualified director on the register was 19.[703] A small 5.9 per cent of directors were younger than 30. The full results of the analysis, grouped by age range, is depicted below for completeness.

Table 13: Frequency table depicting ages (ranged) of disqualified directors on the DDR

Age Range	Frequency	Percentage of total
16-24	78	1.1
25-34	1037	14.4
35-44	2209	30.8
45-54	2272	31.7
55-64	1239	17.3
65-74	313	4.4
75+	30	0.4
	7178	*100.0*

6.18 It must be cautioned however that it cannot be drawn from this data that 'young' directors are either more or less likely to be disqualified than older directors; nor can it be stated that age is a causal factor in disqualification. Such findings could not be made without more data, for instance the total number of directors in those age brackets registered as being directors of active companies at CH. In fact, one would almost certainly (though unscientifically) expect there to be a much higher frequency of disqualification amongst middle-aged directors, simply on account of there being more

[703] There were two directors of that age on the register.

of them. Other factors to consider in approaching the statistics might be that young directors are likely to be accompanied on the board by older individuals, particularly in family undertakings. This supervisory element may reduce the risk of any misconduct occurring (unless the adult herself is errant of course). It may also be the case, though it is not known to be, that the SS is reluctant to pursue minors for disqualification undertakings.[704] There is clearly more scope for research to be conducted in this area.

6.19 The statistics do however go some way in assisting with the question of whether any benefit is likely to be derived from increasing the minimum age. As previously stated, the purpose of doing so in this context must be to further reduce the risk of errant directorship. The answer to that question then must be a resounding 'no' if disqualification is presumed as being a measure of identifying problem directors.[705] The fact that no directors under 18 were on the DDR provides some support for the notion that this demographic are not 'problem' directors, or at least not noticeably so. Whilst it is likely that there are a very small number of this demographic in the first place, this is precisely the point. In the director liability context, it is therefore argued that any negative effects stemming from the inhibitions placed on entrepreneurial freedom in increasing the age is likely to be greater than any derived benefits.[706]

[704] Though, it is not shown that the courts are reluctant to make a finding of liability against a young person; merely that they may impose a lesser period of disqualification.
[705] It has been argued that disqualification is not an effective enforcement mechanism when measured against its objectives. It cannot be said however that it is ineffective as one means of identifying directors who have committed misconduct.
[706] It is recognised that there may be other socio-legal, cultural or political reasons for increasing the minimum age. Such matters, whilst tempting to consider, fall outside the ambit of this thesis.

THE EDUCATION AND TRAINING OF COMPANY DIRECTORS

6.20 The final method of reform considered by this chapter will be as to the possible benefits derived from educating or training company directors. The idea is that, as will be explored in detail, a large proportion of enforcement action is taken against directors who are incompetent and ignorant as to basic management matters.[707] Therefore, in creating a baseline competence of directors, standards of management within limited companies would be raised across the board. If successful, it would reduce reliance on existing *ex post* enforcement mechanisms by decreasing levels of misconduct in limited companies, thereby leading to fewer insolvencies, ultimately to the protection of unsecured creditors. The measure of success must therefore embody all of these elements which, as a secondary benefit, ought to increase the trust and confidence in the enforcement regime.[708] Higher standards of management ought, in turn, to reduce insurance or borrowing costs given reduction of a risk factor.[709] Moreover, a baseline standard ought to reduce the prevalence of 'ignorance' based arguments, either within section 17 CDDA 1986 applications or those substantively on liability or quantum in improper trading or compensation proceedings. There are also wider economic benefits for providers of the training (most likely to be private enterprise), as well as benefits commensurate with upskilling society more generally.

[707] 3.17.
[708] Perhaps even more importantly, trust and confidence amongst the public in wider corporate governance and of directors generally should also increase.
[709] Williams and McGee have also suggested that in one system 'qualified' directors may not be required to give personal guarantees, whereas 'unqualified' ones would. This assumes an implementation where qualification is not the norm. It is also likely an oversimplification as training/education is probably only one (of many) risk factors for consideration: Williams and McGee (n 454) 26.

6.21 The discussion surrounding educating directors is not a new one (though it *is* largely under researched). In fact, recently, as part of the *Transparency & Trust* Consultation respondents were asked to comment on the following issues in this context:[710]

(a) whether, if some form of director education were to be introduced, it would increase trust in the enforcement regime?

(b) what form the training should take and who should provide it?

(c) what would be the likely cost of such training?

(d) whether successfully completing any such training should enable a reduced period of disqualification; or should be a pre-condition for any disqualified director wishing to seek leave of the court to run a company whilst disqualified?

(e) whether there would be value in offering such training to all directors of failed companies – irrespective of whether they were disqualified - having regard to the fact that the director would need to cover the cost?

6.22 The implementation of any form of director training was subsequently abandoned. However, it is important to note that there was generally universal acceptance amongst Consultees that educating directors in and of itself is a good thing;[711] this is surely uncontroversial, and it is surprising that Government made no efforts to address it. Consultees, however, differed wildly as to the possible permutations of implementation and the associated benefits. It is this point upon which the remainder of this section will focus. The author will also attempt to address some of the questions posed by the Consultation, as well as the associated difficulties, before drawing some conclusions as to the potential effectiveness of such a scheme.

[710] T&T Discussion Paper (n 14) para 13.9.
[711] Almost universally; over 80 per cent of those that responded.

Target market

6.23 In considering a system of education and training,[712] the author is reminded of the seminal work on responsive regulation by Ayres and Braithewaite. In that work, the authors commented on an anecdote of a Chester Bowles who reported that:

> 20 percent of all firms would comply unconditionally with any rule, 5 percent would attempt to evade it, and the remaining 75 percent are also likely to comply, but only if the punitive threat to the dishonest 5 percent is credible.[713]

Similar logic it is suggested may be utilised as a lens through which to view directors and their adherence to both good practice and the law[714]. Whilst much of the following discussion is academic in the purest sense, given that it essentially impossible to determine which particular category any given director belongs to (at least until it is too late), it is interesting to consider in this context.[715] Firstly, it is argued that the demographic who would derive the most benefit from education must be the '75 per cent'. The '20 per cent' is made up of those directors who will always obey the law as well as adhere to good management practices. Education would not particularly benefit this group of persons as there is no predisposition to commit misconduct. If education programmes were to be voluntary, this portion of directors would attend in greater numbers. Put simply, this demographic is keen to understand new developments in the law and better ways to manage their business – in the spirit of continuing professional development – although statistically they are the ones least likely to be disqualified, in

[712] For present purposes the words 'education' and 'training' will be used interchangeably.
[713] Ian Ayres and John Braithewaite, *Responsive Regulation* (OUP 1992) 25.
[714] Though the reader will understand that it is not intended that Bowles' percentage figures can be transplanted in to this context and expressed as a reliable indicator of the actual numbers involved. There is no point in attempting to be too precise about this, given that an accurate survey would be extremely difficult to conducted.
[715] Bardach and Kagan express a similar notion that '[t]en percent of the firms cause 90 percent of the problems'. Again, this 90/10 distribution is used merely for illustration; though the reader no doubt understands the general gist of the point. See Eugene Bardach and Robert A Kagan, *The Problem of Regulatory Unreasonableness: Going by the Book* (Transaction Publishers 2010) 66-67.

part due to their attitude towards risk taking. Conversely, there will undoubtedly always be a thoroughly dishonest proportion; Bowles' '5 per cent'. These are directors that intentionally set out to be fraudulent or otherwise. For this class of individuals, it is similarly suggested that no amount of training or education is likely to be of benefit. They are simply dishonest and never able to be rehabilitated. As such, these individuals ought to suffer the full extent of the sanctions that the law can offer. That does not mean, however, that they should not receive any training at all as there may be some general benefit.[716]

6.24 This then leaves the '75 per cent' demographic as those most likely to benefit from the implementation of training requirements. The reader is reminded that the non-payment of Crown debts and accounting misconduct account for the vast majority of director disqualifications. As has been argued, in many cases this is as a result of incompetence (rather than wilful dishonesty). Moreover, awareness of enforcement mechanisms is low, thereby reducing the deterrent effect.[717] The category of persons afflicted by incompetence and ignorance, it is suggested they being primarily within the '75 per cent', are those that stand to gain the most from training. In theory, it should reduce levels of incompetence and ignorance by definition. As such, it is argued that it presents a credible mechanism for reducing misconduct if properly targeted towards this demographic. It should be noted by way of limitation, as Finch explores, that

---

[716] For example, it may assist in determining culpability or reduce the likelihood of successful arguments of ignorance. This may arise in the context of determining the period of disqualification or CDDA 1986 s 17 applications. More broadly, where liability is to be apportioned across multiple individuals, it may arise in determining the extent of any particular individual's liability.
[717] 2.11.

'training does not guarantee competence'.[718] This is a truism; history has seen its fair share of entirely incompetent professionals across all sectors. The object however is not to entirely defeat misconduct. This would be little more than a pipe dream. The object is instead to implement a targeted training effort which minimises the risk of incompetence-based failure. A primary factor in the resulting effectiveness of any training system, it is submitted, is however heavily dependent on the real-world proportion of the '75 per cent'. Put simply, how many directors fall within this demographic? Any realistic determination of that question is likely resigned to the impossible.

Existing Provision

6.25 A few words should be said about the existing provision of education and training for directors. There are no minimum educational requirements for company directors. As such, it generally falls to each given individual to determine what level of training they require, if any. Bodies such as the Institute of Directors (IoD) offer high-level qualifications, such as their 'gold standard' Chartered Directorship.[719] There is also the more traditional route of attending a higher education institution, many of whom provide degrees in management including the coveted MBA.[720] At the other end of the spectrum, there are numerous training courses offered by private providers for those

---

[718] Vanessa Finch, 'Company Directors: Who Cares About Skill and Care?' (1992) 55(2) MLR 179, 210.

[719] For full details see the Institute of Directors, 'Chartered Director' <http://bit.ly/2toupz1> accessed 1 January 2017.

[720] The 'Master of Business Administration'. The Complete University Guide suggest that this qualification can cost anywhere between £16,000 and £73,000 in the UK: The Complete University Guide, 'MBA' <http://bit.ly/2tXQYrw> accessed 1 May 2017.

new to managing a limited company.[721] Moreover, CH themselves offer free workshops across a variety of topics (including one for new directors) should directors choose to take advantage of them.[722] There is a considerable amount of information on various Government websites as to directors' duties; enforcement mechanisms; submitting confirmation statements; preparing and filing accounts; company and insolvency law generally; as well as how to seek help if in difficulty.[723] One should also not forget the initial information leaflet on directors' duties sent out to all directors on appointment by CH.[724]

Voluntary or Mandatory?

6.26 The problem, then, is that whilst there is some provision in the marketplace already, if directors are left to police themselves and are given a choice as to whether they should incur additional training costs, a considerable proportion will simply not bother. As Finch notes, the IoD revealed in 1990 that less than 10 per cent of directors had sought out any training whatsoever.[725] Moreover, less than 25 per cent possessed any professional or managerial qualifications.[726] Those that do seek out training voluntarily probably belong to the '20 per cent' demographic and therefore, save for the

---

[721] The Institute of Directors for instance provide a number of training courses, including the Certificate in Company Direction. For full details see Institute of Directors, 'Training' <http://bit.ly/2tkn3Mm> accessed 1 January 2017.
[722] The CH 'First Time Director Seminar' is a free of charge 3–hour seminar ran nationwide, details of which are published on the CH website, see: <http://bit.ly/2t0mLrW> accessed 1 May 2017. Its title is however somewhat misleading. The aims of the seminar are set out to be: (a) explain how to easily and securely send information to CH; (b) inform how to prevent corporate identity theft; (c) inform about CH compliance; (d) make you aware of changes to the CA 2006; (e) demonstrate how you can search and use CH information. Whilst these issues are no doubt important, the author queries whether the aims of the syllabus are properly focused given current levels of misconduct.
[723] The sources are too numerous to recant. However, the websites of CH, DBEIS, and IS contain a vast quantity of information in this respect.
[724] Though no other known steps are taken.
[725] Institute of Directors, 'Professional Development of and for the Board' (January 1990) as found in Finch, 'Company Directors: Who Cares About Skill and Care?' (n 718) 210.
[726] ibid.

intrinsic value of the education itself, would derive very few wider benefits from it. Incidentally, in the same survey conducted by the IoD they noted that only 24 per cent of respondents considered training 'very important'.[727] On any implementation of a training scheme, then, little needs to be said on the subject as to whether it should be a *requirement*. For the reasons set out, it is submitted that a mandatory scheme is the only credible way forward. This may seem to be a restrictive approach. But, even in a mandatory system, it should not be forgotten that a person wishing to avoid formal training could simply trade on an unlimited liability basis. Of course, there would need to be some carve outs, for example, for established professionals. Practising barristers, solicitors, accountants, and those in related professions, should be exempt. Those with undergraduate or higher degrees in relevant fields (for example, law, business, management, and accountancy) might also be exempted. In terms of wider-reaching impact, it might also be suggested that the course content of those degree programmes ought to include the elements covered within the director training, and this could indeed be used as an additional marketing tool by education providers in recruiting students.

Who Should Pay?

6.27 Training has a cost, but if successful there are long-term prospects for a good return on investment. The answer as to who foots the bill falls into two camps; either the director, or the taxpayer. It is only justifiable that the taxpayer should pay where it can be shown that any outlay is offset by a reduction in economic loss caused through misconduct and subsequent insolvencies. Politically, however, convincing taxpayers that they should pay for director training is a hard sell. If directors are to pay, and it is

[727] ibid.

argued that this is the most pragmatic approach, then minimising cost and maximising value is essential. It would be a sorry state of affairs if training came to be viewed as a mere 'price to pay' to manage a company; for the preserve of the wealthy or those with large capital injections. Instead, a shift in culture is necessary: training should be viewed as an essential start-up cost in the same way that incorporation itself is.[728]

Content

6.28 Sessions would need to be highly practical and pitched at a level that could be understood by the uninitiated, but sufficiently detailed so as to deliver the necessary information. The course content and delivery should be consistent across all delegates, to ensure that a minimum baseline standard for directors is achieved. The more content that is covered, the greater the time and cost incurred. As such, a consultation process would need to be undertaken to realistically appraise what this minimum baseline standard ought to require. Common matters leading to a finding of 'unfitness' would be an obvious starting point. It is suggested that training ought to cover at minimum: directors' duties; a recognition of enforcement mechanisms and potential ramifications; insolvency basics and how to seek advice when things go wrong; record keeping; CH requirements including confirmation statements; and basic tax matters, with a particular focus on corporation tax and VAT. It is recognised that this is not a short syllabus. That is why considerable energy would have to be directed into thinking about what is *essential*, with the object of preventing misconduct in mind. This should be left to the hands of organisations expert in this field, not Government. Several consultees

[728] As an aside, the author is slightly unsympathetic to those that could not afford even the most modest training costs. There are considerable issues with allowing such people access to the corporate form in the first place. How would they be able to properly capitalise a company, pay accountants fees or insurance, for example? Let us not forget that in default they would always have the alternative of trading on an unlimited basis.

suggested that the IoD would be well-equipped to carry out such an inquiry, and develop an appropriate syllabus at reasonable cost. This seems like a sensible suggestion.

Possible Implementations

6.29 The reader will appreciate that the number of possible permutations of implementation are infinite. However, some general observations will be made, with a particular focus on some of the key matters raised by Consultees.[729] It is suggested that there are three primary variables for consideration in designing the training scheme: cost, time to complete, and value obtained.[730] Against the backdrop however there is always the pressing concern that a system too restrictive would have a negative economic impact and be a barrier to entrepreneurship. It is therefore desirable to find a balance so that the maximum possible value is extracted, albeit within a reasonable time, for a sensible cost.[731] An initial problem relates to whether the training should lead to an accreditation or qualification following examination; whether it should merely be attendance-based; or whether a 'lighter touch' is sufficient. The author has set down some of the most commonly advocated implementation types based on Consultation responses:

[729] One other issue not covered here, but raised by Consultees, was the prospect of differing educational requirements depending on the sector and/or size of the company. This type of approach would require directors of a growing business to continue in their training as time and expansion goes on.
[730] Value here is defined in the wider sense, i.e. not just the intrinsic value of education to the individual, but the wider societal value in terms of increased public trust and confidence, less misconduct etc.
[731] Though it is recognised an exact balance is a utopian dream.

Figure 3: Director Education: Implementation Types

Type	**Implementation**
'Light Touch'	Warnings during online incorporation
	Publication of online materials (including videos) by CH or DBEIS
Attendance Based	Seminars and workshops
	'Director Awareness Course'
Accreditation	Remote learning with online testing
	Provision of course materials, with computer or paper based invigilated examinations
	Full Regulatory body style accreditation (similar to FCA)
Qualification	NQF recognised Certificates and Diplomas etc.
	Professional Director Qualification (e.g. Chartered Directorship)
	MBA or similar

The further one advances through the list the potential value to directors increases; as do the cost and time variables. An MBA or other Masters level qualification requirement is entirely disproportionate.[732] It is a foregone conclusion that there would be very little appetite for 'professionalising' the company director. At the other end of the spectrum, whilst the simple publication of materials online would be an incredible resource (and should be adopted in any case[733]) they are less valuable in this context as they rely on director awareness and instigation; essentially the system already in place. It is argued here that the optimum position likely lies somewhere in between. Namely, some form of Director Awareness Course (DAC) and/or online testing which leads to being named an 'Accredited Director'. The obvious distinction between the two is that

[732] Similarly, whilst Chartered Directorships are no doubt incredibly valuable, the target market for these is the well-established professional. For the average director, it would be the case of a sledgehammer cracking the nut.

[733] For instance, two Consultees suggested that DBEIS publish videos on directors' duties and enforcement mechanisms as a public resource.

one is attendance-based, i.e. there is no testing of knowledge or competence. Turning up is enough. It is worth noting that the IoD, as part of its Consultation response, set out that it could provide basic level training for £300-400, or more comprehensive training for £1000. They did not, however, state the specifications of that training, i.e. the type of implementation, whether it was competency tested, the syllabus etc. One option is to model the DAC upon the existing ‘Speed Awareness Course’.[734] An eligible driver who successfully attends (and actively participates in) the course will suffer no other punishment, it being an alternative to prosecution. The courses are paid for by the driver. An obvious problem with any attendance-only course is that whilst it may have intrinsic value, it is only effective if it is taken seriously by those attending. It is plausible that a culture may develop of it being seen as ‘a hurdle’ to overcome to become a director, but nothing to be concerned about; a mere formality. Moreover, those who *do* take the course seriously are probably those who are less likely to commit misconduct in the first place. A DAC therefore has a number of significant limitations. As such, it is this author’s view that the only credible option is to implement some form of testing.[735] This could take various forms. Again, at the low end of the spectrum it could be an online multiple-choice test[736] (or similar) provided by CH through a secure portal. This has the benefit of being cheap to provide, maintain and score. Results could be delivered instantly. The downside to this approach is that impersonation on tests

[734] Essentially, these are group-based interactive workshops aimed to ‘reduce casualties, encourage greater compliance with the law and good road use, and offer a behavioural change intervention’ amongst other things: see Department for Transport, ‘Effective Interventions for Speeding Motorists’ (2006) available at <http://bit.ly/2tkw2x5> accessed 1 June 2017 para 7.2.1.

[735] Philip King, chief executive of the Institute of Credit Management is also amongst those who has stated he would ‘favour a qualifying examination before directors could obtain limited liability protection’, though he concedes it is unlikely to happen any time soon: Houghton (n 694) 46.

[736] While multiple choice questions are often seen as a ‘soft option’, properly crafted questions can test *application* and not merely knowledge. For example ‘single best answer’ type questions, can be made as complex (or easy) as is necessary.

could become rife, and questions from the database are likely to be leaked and discussed online. The better alternative, to ensure integrity of the assessment is to have an invigilated examination, perhaps modelled on the Driving Theory Test. This comes at a greater cost but, to give some context, the current theory test is a mere £23.[737] It is a computer-based exam taken at an invigilated assessment centre consisting of, in part, a multiple-choice element. The pass score for the test must be realistic, yet not undermine its function. Successfully passing the test should lead to the individual in question being named an 'Accredited Director' and assigned a unique identifier at CH which permits appointment to any number of companies. An individual who fails should be permitted to re-take the test.

6.30 Though considerable consultation would have to take place on the proper implementation, it seems to this author that for cost reasons one workable solution would be to offer a series of self-study modules utilising online videos and information, or hard copy materials for those that prefer (at an increased cost). Videos should be delivered by practitioner and academic experts, in line with the devised syllabus. Following completion, the individual could enter themselves for a computer-based test at an assessment centre. It is argued that this implementation would balance the three variables of time, cost and value. It would not require attendance at workshops, which may be impossible for some, and massively increase costs. Whilst the absence of face-to-face training would impact upon its value it is argued that the necessary information

[737] Though, due to the smaller numbers involved in educating directors, it is recognised that these costs are likely to be higher.

is perfectly capable of being conveyed in this way.[738] Moreover, it has the benefit of allowing individuals to replay and revisit content until the concepts are fully understood.

When to Educate?

6.31 One of the most important considerations that has not yet been dealt with is a simple one: when do you train directors? It is argued that training pre-appointment is the best, though not the only, way forward. The Consultation itself sought opinions on educating directors as part of the enforcement regime, i.e. post-failure or post-disqualification. Mandatory training targeted at the disqualified is inherently attractive in common sense terms as it deals directly with those who have been identified as problem directors, as opposed to implementing a more pervasive system that deals with both good and bad apples; arguably to the inconvenience of the good. As will be explored, however, there are inherent difficulties with this demographic. The author therefore ultimately concludes that training *all* directors before first appointment is the optimal position, as it ensures the benefits of creating a minimum baseline standard across the board are felt. The points in time at which training becomes desirable are not always mutually exclusive. It may be appropriate to train a director both on appointment and *re-train* her post-failure, or post-disqualification. The next section of this chapter intends to deal with the arguments that arise out of these considerations, including educating directors on appointment; as part of continuing professional development; post-disqualification and post-failure.

[738] Indeed it is the future, with many traditional undergraduate lectures likely to be phased out by an online alternative. See Rhett Allain, 'The Traditional Lecture Is Dead – I Would Know I'm A Professor' *Wired* (11 May 2017) <http://bit.ly/2pDzZs9> accessed 1 June 2017.

Education post-disqualification

6.32 We now return to the driving analogy, though this time with a focus on *disqualification* from driving following errant behaviour. A marked distinction between drivers and directors is that the driver who commits misconduct is generally dealt with under the ambit of the criminal law[739], the latter usually under civil law.[740] Disqualification for a given period is merely one of a range of sentencing options available to deal with miscreant drivers.[741] The three objectives of disqualification from driving are restraint, deterrence and retribution.[742] Safeguarding the public against further breaches of road traffic law is crucial (i.e. restraint), whilst acting as a deterrent to further misconduct, thereby improving driving standards, is an important secondary aim.[743] In short, there is considerable similarity between the objectives and effects of disqualification in both contexts.[744] However, the means of going about rehabilitation could not be more different between the two. Drivers who are disqualified, save for in the most minor instances, do not automatically regain their driving licence following the lapse of the disqualification period. In the case of more serious offences, drivers must reapply for a licence, and ultimately pass a further (for the most serious offences,

[739] This is largely pursuant to the Road Traffic Act 1988. The reader is reminded of the general power of any criminal court (excluding court martial) to disqualify a driver, upon sentencing, pursuant to the Powers of Criminal Courts (Sentencing) Act 2000, s 146. Surprisingly, the power can be exercised even where the offence in question does not involve the use of a motor vehicle.
[740] Largely by way of the mechanisms discussed in this thesis.
[741] In fact, again to contrast with director disqualification, it is often used as an ancillary measure to be combined with fines or imprisonment in the most serious of cases, as well as other ancillary sentencing options such as victim surcharges. Director disqualification, given that most are by way of undertaking, tends to stand on its own; though this seems likely to change given the introduction of compensation orders and undertakings. 2.34.
[742] Catriona Mirrlees-Black, *Disqualification from Driving: An Effective Penalty?* (Home Office Research and Planning Unit, Paper 74, 1993) iii.
[743] In the driving context, it would appear that as a specific deterrent is effective in many cases, though awareness of disqualification as a potential punishment was rather low. See: Mirrlees-Black (n 742) 36.
[744] As to retribution, it has been previously argued that directors' disqualification is in large part a punitive mechanism that ought properly to be dealt with by the criminal courts: 2.6.

extended) competency test. To pass the test, disqualified drivers will invariably have to seek training from an approved driving instructor to re-skill themselves to the required standard. In contrast, disqualified directors can return to office immediately following the lapse of their disqualification without further let or hindrance. This is remarkable. It is nonsensical, even though raising standards of management is an aim of the regime, that directors are not compelled to undertake training before being allowed to return to office after their period of disqualification lapses.

6.33 One option therefore is to require training for directors wishing to return to office following a lapsed disqualification. This was an idea specifically considered in the Consultation:

> [The Department is] not aware of any evidence that a director who has served their period of disqualification will return to the market better equipped to act in the management of a company than before. This suggests that the public interest may be better served by offering disqualified directors the opportunity to undertake some form of education or training, helping them to take positive steps to learn from previous mistakes.[745]

Ultimately it was rejected. The Government Response to the discussion paper suggested that educational requirements would be a 'disproportionate response because of the risk of burdening UK companies'.[746] Many consultees were however in favour of training as a pre-requisite for those seeking return to office post-disqualification.[747] Many others felt, without additional training requirements on appointment, it did not go far enough and would be unlikely to increase trust and confidence in the enforcement regime.[748] In

---

[745] T&T Discussion Paper (n 14) para 13.6.
[746] T&T Government Response (n 223) para 194.
[747] It is also of interest that over 30 years ago, during the passage of the Insolvency Bill in 1985, Lord Meston raised similar arguments: 'I would go further and say that the burden should be on the disqualified director, once disqualified, to show that he is fit to be allowed back into the commercial ring.': HL Deb 15 January 1985, vol 458, col 915.
[748] Some 60 per cent.

the words of one Consultee, it was simply 'too little, too late'. This author agrees with those sentiments. One key issue however is market re-entry. If to be considered a viable means of addressing director misconduct, some thought must be given to *how many* directors seek to take up a directorship following the lapse of their disqualification. Evidently, should the frequency of re-entry be low, the benefits of educating this particular demographic is questionable. The time and cost associated with designing and implementing a targeted form of retraining is likely to be considerable. It therefore seems to this author that the whole point is diminished into insignificance should it be shown that appetite is comparatively small. Returning to the disqualified driver analogy, it is suggested that one of the primary reasons that a period of re-training and additional testing works in this sector is that there is a high rate of re-entry to the market post-disqualification. Therefore, a considerable public interest exists in retraining formerly disqualified drivers to reduce casualties, improve driving standards, and promote best practice when (as it is submitted most probably do) they return to road. As will be demonstrated, however, the same does not necessarily hold true for company directors. In fact, as will be uncovered from the ensuing analysis it is the conclusion of this author that the implementation of a system of post-disqualification education, in isolation, is of limited value for this reason. The next part of the chapter will therefore consider the following question: how many directors re-enter the market once the period of their disqualification has lapsed?

6.34 *Methodology* The reader is reminded that the DDR obtained by this author contained a list of every disqualified director as at November 2013.[749] On 1 February

[749] 3.5.

2017, the author set about utilising the DDR for the purposes of understanding and evaluating how many of those disqualified directors had chosen to re-enter the market following the lapse of their disqualification order or undertaking. The reader will remember that the DDR contained 7,825 records of disqualified directors, with each record consisting of a range of biographical and disqualification related data:[750] Additional analysis had to be undertaken for present purposes. The following actions were carried out to the DDR to create a new dataset:

(a) given the focus of this thesis on the law and position in England and Wales, 552 records pertaining to directors disqualified in connection with the activities of Scottish and Northern Irish companies were removed;

(b) all records where the disqualification expired *after* the date of the analysis, that being the 1 February 2017, were removed. This resulted in the removal of 3,363 records;

(c) a further 4 records were removed where the recipient of the disqualification was a corporate body as opposed to a natural person;

(d) 17 duplicate entries were removed.

The final sample for analysis comprised 3,889 records.

6.35 The author then proceeded to write a computer programme[751] which queried the CH live database of company directors as at 1 February 2017. The database contains data as to all[752] company directors, both those active and those who have resigned from office (whether following disqualification or otherwise). Since the initial DDR data was obtained the register has been reinvented and improved, albeit it remains in a beta testing phase at the time of writing. One major improvement, enabling the present study

[750] See 3.9 for a list of the data extracted. For some records, not all of the aforementioned data was available though in each case enough 'core' data was available to be able to accurately identify the director in question.
[751] Enabled by his background in Computer Science
[752] Though on the use of the word 'all' see the section in this chapter on limitations of the study, below at 6.37.

to be undertaken, has led to every director being associated with a unique identifier.[753] All companies of which the individual is either a director or secretary are linked to that identifier. Determining an individual's identifier, assuming the accuracy of the database, then permits the researcher to display a list of all companies for which a person acts as a director or secretary.

6.36 The object of the programme therefore was to search the database for a record of each of the 3,889 directors in the dataset. In matching each of the records with a corresponding record on the live database, it would then be possible to determine whether any particular individual was at present recorded as having an 'active' company directorship. It was also possible to use the records relating to their association with the company which led to their disqualification to further ensure the accuracy of the results. The analysis proceeded on the basis that if an individual appeared on the live database as having an 'active' directorship, then that person *had* returned to take up a directorial position following the lapse of their disqualification. The directors were traced using the company number associated with the disqualification or, where this was unavailable, their full name, date of birth and location. A total of 807 directors of those queried were not listed on the database whatsoever. For this analysis, these directors were removed from the sample.

6.37 *Limitations* Given current governmental attitudes to director education it is submitted that the possibility of a wide-reaching inquiry into this area is unlikely in the short to medium term, hence the present study. However, the author recognises the limitations of the analysis carried out. As such, the reader should consider the insight

---

[753] For example, the author's identifier is v2I946iQuBkw8mRrvm4gfHhY6OI.

provided as something of a valuable 'snapshot' of market re-entry rates at the exact moment the data was gathered though, until the full extent of the raw data becomes available, nothing more. Firstly, the validity and reliability of the data is very much consequent on the source material being accurate and complete. As set out, some 807 directors known to be disqualified were simply not listed on the database. Whilst the reason for this is unknown, it may be a result of systemic error or oversight in the CH process of data migration from the 'old system'. As such, it cannot be stated conclusively whether the data that *was* available was by any means accurate. On balance, however, it is submitted that it is of sufficient integrity for present purposes. Secondly, the CH database is currently marked as being in the 'beta' stages of development. It is assumed that this refers to its functionality rather than the integrity of the actual data held, though again this cannot be conclusively stated. Thirdly, it is unknown as to whether the CH unique identifier system is capable of associating records of directors who have changed their name. For example, a director who changes her name and is appointed under that new name is likely to be assigned a new 'unique' identifier, unless CH has a means of determining former names of directors and associating them within a single identifier. The practical implication of this for the survey is that the proportion of those directors who re-enter the market may be either over or under represented where a director changes their name following disqualification (through marriage, taking on an alias, or otherwise) and therefore is rendered unidentifiable.[754] Fourthly, by way of a further limitation relating to the development of the computer programme, it is also possible that some directors were

[754] For instance, it is highly likely that some proportion of the 807 directors who were unable to be traced on the database have merely changed their name and are thus unable to be identified.

mistakenly identified and collated into the survey data erroneously. However, the author only collated records (all others being excluded) where it could be shown that a director with the same name, date of birth and (in some cases) place of residence, as taken from the November 2013 DDR was present on the February 2017 online system. As such, it is suggested that the risk of this having occurred is small.[755] Finally, but importantly, the timing of the two data sets must be explored. The NAO has stated that, based on its own research, a company director is most likely to be involved in a second corporate failure within five years of the first.[756] Given that the disqualifications on the DDR lapsed at different times, the closer to February 2017 that they lapsed, inevitably the 'less time' those directors had to re-establish themselves in the market. For instance, a director whose disqualification lapsed in December 2013 will have had approximately 38 months in which to return to a directorship. On the contrary, a director whose disqualification lapsed in January 2017 will have had merely 1 month to do so. Both will have been caught within the sample data. It therefore seems clear that the utility of the data must decrease as the end date of the disqualifications tends towards February 2017. It is for this reason that it was previously stated that the analysis should be viewed as nothing more than a 'snapshot' into market re-entry statistics. The most reliable approach would be to examine a large sample of disqualified directors exactly five years following the lapse of the order or undertaking. For present purposes, this is simply impossible to carry out; though it would provide a more accurate insight into the number of directors who have since re-established themselves, as well as those who have suffered multiple corporate failures. Therefore, until a more expansive survey based on

[755] Simply because in the vast majority of cases the director in question was identified by his or her connection to the company leading to the disqualification.
[756] NAO Follow-Up Report (n 15) paras 19-21.

the raw data is forthcoming, it is argued that the author's survey provides a valuable indicator if nothing more.

6.38 *Findings* There were 3,082 records for which unique identifiers could be obtained. The details for each of these directors could then be matched against a record in the CH database. Out of this number, 2,158 directors were listed as having zero current appointments. This left 924 records for which it was indicated there was one or more current appointments. Out of this proportion, 381 directors were exclusively appointed to a company or companies (excluding the company leading to their initial disqualification) that were listed as being 'inactive'.[757] The remaining total of 543 directors were listed as being directors of one or more 'active' companies. The analysis carried out therefore reveals that:

(a) 30.0 per cent of directors in the sample had at some point returned to manage a limited company following the lapse of their disqualification[758];

(b) 58.8 per cent of those (17.6 per cent of the total records) were considered to be directors of 'active' companies;

(c) Therefore 41.2 per cent (12.4 per cent of the total) of those were directors of solely 'inactive' companies. This suggests that approximately two-fifths of those who returned to a directorship post-disqualification had suffered at least a second (or greater) insolvency.

6.39 Perhaps surprisingly then, the figures indicate that a considerable majority of directors do not return to the marketplace. It is unclear whether this is due to reluctance,

---

757 This is a status attributed by CH to a company that is in a formal insolvency regime, is in the process of being wound up or is otherwise not 'active'.

758 That is 70 per cent did not. This perhaps highlights further issues as to the suitability of disqualification for dealing with misconduct in the long-term if a result a considerable majority of do not return to the market place. Some may argue that it is in the best of interests of wider society that problem directors do not return. Others may interpret disqualification as creating an undesirable chilling effect in relation to the management of future companies. If the latter, clearly this is counter to the original aim and purpose of the disqualification regime as a whole, i.e. as being non-punitive. A further study as to the lost economic benefits from removing these directors from the market place would no doubt prove interesting.

continuing to trade in an unlimited form, a chilling effect, or otherwise. In any case, the relatively small numbers involved render it questionable as to whether the time and expense associated with implementing training for solely this demographic is worthwhile. It is submitted that it is probably not.[759] As such, the original argument is reiterated: implementation must be 'all or nothing' to see the benefit. Moreover, it must be remembered that purpose of this chapter is to suggest *ex ante* reforms, therefore to do any differently merely returns us to the original problem of being reactive, rather than proactive. It also lends itself to the (untested) assumption that education would in some way prevent repeat offenders.[760] If, however, Government was minded to undertake a 'trial' of some form of training it is submitted that disqualified directors would be an ideal demographic for initial focus with longer-term prospects of rolling it out to all directors.

6.40 *Other Matters* One suggestion coming out of the Consultation was that training post-disqualification ought to reduce the period of disqualification, thereby providing further incentive to undertake it.[761] It is argued here such an approach must be firmly rejected. Firstly, as has been shown, the rates of market re-entry are not particularly high. As such, there seems little worth in incentivising directors to take up education given that many are unlikely to be interested. Secondly, taken to its logical conclusion this in effect amounts to a person being able to 'buy' their way out of sanctions. This is undesirable both politically and in terms of increasing trust and confidence in the

[759] On the latest statistics for 2015-16 there were 1,327 disqualifications. 30 per cent would account for approximately 398 directors who might face compulsory training in any given year. See: CH, *Companies Register Activities 2015-2016* (n 666) Table D1.
[760] Although education should prevent repeat offending, in theory, unless the individual is part of Bowles' '5 per cent' as discussed previously.
[761] This approach again assumes a voluntary implementation.

enforcement regime. To paraphrase one Consultee, the purpose of education should be to avoid failure *not* to avoid disqualification. Another Consultee took the position even further, stating that those with existing training should face an additional layer of sanctions. The author has some sympathy with that view in respect of qualified professionals, such as lawyers and accountants who act as directors, but then fall to be disqualified due to matters within their expertise.[762] However, in the event that a baseline level of education is implemented, by definition all directors should be of a similar minimum standard and such an approach would be unwarranted. It also must be the case, given the minimum two-year period for disqualification under section 6 CDDA 1986, that directors disqualified for the minimum period would have no incentive to undertake training; as the court would be unable to reduce the level of sanction any further. A separate argument arises as to the impact of training upon section 17 CDDA 1986 applications. One consultee suggested that the section should be abolished due to its current effect of undermining trust and confidence in the enforcement regime. Others suggested that it should be heavily curtailed in respect of requiring a director to undergo a period of training or rehabilitation as a pre-condition to granting the application. If section 17 is to remain, this seems a sensible option. To ensure it has sufficient bite, directors who fail to adhere to their training requirements should be found guilty of contempt.

6.41 As part of a wider training package, as is advocated, there would be no impediment to a director having to carry out further training following disqualification– as is the case with driving. A director who has undertaken initial training but then falls

[762] This is already the current practice. It is most noticeable where there are multiple directors and it is a case of apportioning blame. See 2.7.

to be disqualified should, it is argued, be required to re-take the same initial training and perhaps a specific type of training relating to the matters for which she was disqualified. Given that this custom training would be targeted at a much smaller demographic and that matters leading to disqualification are largely centred around similar themes, it would surely be workable for providers to cater for this. Moreover, it would be incredibly valuable given that it would deal directly with the problem behaviour.[763]

Education post-failure

6.42 There is some merit in the argument that educating directors post-failure may be an optimum middle ground. It has the advantage of dealing with those that have a proven track record of failure, but does not disadvantage the general population of directors (some of whom might never fall foul of the law) by requiring training across the board. However, this author would resist such arguments again on the grounds that it does little to improve the situation for unsecured creditors in the short-term. The NAO's finding that a director is most likely to face her second failure within five years,[764] means there is likely some appetite for this approach. However, there is no current data as to how many directors post-failure (but without being disqualified) re-enter the market. Moreover, one needs to look at the general tax/accountancy defaults as being the reason for most disqualifications. It cannot be said with any certainty that a similar proportion of actual failures are a result of such matters. But, if they are, then they surely ought to be taught and understood from day one; there seems little point in

[763] However, such an implementation still suffers with the difficulty of relatively low numbers of market re-entry.
[764] NAO Follow-Up Report (n 15) paras 19-21.

attempting to remedy poor accounting and management practices after the event, once bad habits have been formed. As with training post-disqualification, however, there is considerable merit in suggesting that directors should have to re-take the original competency test post-failure as part of a rehabilitative process.

Education on appointment

6.43 Driving has been used throughout this chapter as a means of comparison. It is well known that drivers are subject to a multitude of education and training requirements.[765] This is because driving is a serious responsibility. Government recognises the need to train drivers in part because, at one end of the spectrum, reckless or dangerous driving can cause death. Initially, a series of competency tests must be passed to obtain a licence, at which point the holder can drive in accordance with that licence, subject to road traffic law. Directors too command significant (and increasing) responsibilities. But, as discussed, most directors undertake no training whatsoever. It does not seem radical to suggest that directors ought to undergo some form of training as a pre-requisite to appointment. In the case of drivers, the rationale is to create a baseline standard of drivers, ultimately to prevent loss of life. In the case of directors, the public interest element is in reducing misconduct, levels of corporate collapse, and ultimately protecting creditors. Training also increases awareness of sanctions, and therefore acts as a deterrent. It is argued that, due to the concerns expressed previously, a system of training which is simply reactive is insufficient to achieve this aim. Testing competency on appointment is the only means of ensuring that all of the associated benefits of training are realised. Given that a considerable proportion of enforcement

[765] See for example the Government webpages on current training requirements, Gov.UK 'Learning to Drive' <http://bit.ly/2s23fKa> accessed 1 June 2017.

action is taken against directors who could likely be rehabilitated, it is simply insufficient for Government to adopt a 'sink or swim' type attitude.[766] Directors who get it wrong should be disqualified, but then they should be helped in their rehabilitation efforts so that they can try again. This is, in fact, not only economically desirable but it is an extension of UK rescue culture. Obviously, this is the most pervasive option and therefore the most difficult to orchestrate successfully. However, it is suggested, firstly, that the potential benefits make it a worthwhile endeavour. Furthermore, any partial implementation is simply unlikely to be effective for the reasons set out. In short, it would be a waste of time and money.

6.44 A wider concern in this respect arises as to whether directors already appointed would be required to undertake training. Whilst this is the optimal approach, it is recognised that it may not be workable in reality.[767] As such, this author suggests that existing directors would not be required to undertake training, however, given that it would apply for all *new* appointments, should that individual wish to become a director of a second (or greater) company then the training would be mandated before that appointment could be confirmed. This has the effect of balancing the impact on existing directors but ensuring that, over a period of time, the baseline minimum standard is achieved and unaccredited directors are phased out.

Continuing educational requirements

6.45 Some Consultees went as far as to suggest that directors ought to have continuing educational requirements, either on an annual basis or some other period.

[766] An argument also made in Freedman and Godwin (n 281) 233.
[767] Presumably it would be implemented so that on an appointed day all unqualified directors ceased to hold office. Given how pervasive such changes would be, there is great potential for calamity in such an approach.

This is a very similar idea to Continuing Professional Development, as required by many professional regulators. Usually, activities will include workshops, seminars or other educational events to ensure professionals are aware of the latest developments in their field. Whilst the author does not disagree with this idea in principle, one has to be realistic. It seems likely that the continuing costs of training for small company owner-managers would prove too much. It is therefore argued that this would be one step too far. However, there should instead be an onus on DBEIS, CH, IS and other relevant Government bodies to periodically distribute plain English leaflets (whether in electronic form or otherwise) to all directors setting out new developments in the law, or changes in practice. This is already done to some extent at present. However, distribution needs to be more widespread. Moreover, directors may struggle to understand *new* developments if they don't have any existing knowledge to build upon. Implementing a minimum baseline standard ought to rectify this issue to some degree.

CONCLUSION

6.46 In summary, then, the problems associated with permitting more or less totally unrestricted access to limited liability cannot be overstated. As has been shown throughout this thesis and intimated in this chapter, much of the burden in relation to this falls at the feet of the small, undercapitalised, owner-managed company. The author has identified that some of the problems can be attributed to the utilisation of solely *ex post facto* enforcement mechanisms. In response, the Government needs to be more proactive in its efforts. Several means of doing so have been analysed, many of which have been ultimately discredited. However, one particular method targeted at the individual director – education on pre-appointment basis – is largely an unexplored landscape. Whilst it gained some traction in numerous responses to the Consultation, it was ultimately rejected without much consideration or published analysis. This is a missed opportunity. Imagine a person, equipped with a scalpel, permitted to operate without satisfactory qualifications or experience; or the motorist allowed free reign of the road system without passing a competency test. A system that would seek to condemn these hypothetical individuals following a transgression seems implausible, but this is precisely the system within which directors find themselves. Government instead takes the extreme stance of ensuring the promotion of industry by freely offering limited liability at any cost, and sees education as a stumbling block in this endeavour. It is argued that this should be revisited, as mandatory training has the potential to bring about considerable cultural change. Most importantly, this shift ought to be an effective force in reducing misconduct. As such, the reduced reliance on *ex post* mechanisms should serve to rebalance the economic factors as to the cost of misconduct and the benefits derived from entrepreneurship. There can be no better recourse for protecting creditors than prevention itself. Perhaps now is the time for a fresh approach.

7

CONCLUSION

7.1 It must be remembered that the starting point is that the regulatory mechanisms discussed throughout this thesis, whether public or private, are designed to curtail to the negative implications of the abuse of limited liability. This need arises due to the inevitable moral hazards created by such unfettered and uninhibited access to the corporate form, as is the current position in UK enterprise policy. As has been demonstrated, this moral hazard is particularly noticeable in the owner-manager context and, indeed, although not necessarily causative, it is that demographic that suffers the vast majority of enforcement action. The operation of the current regulatory regime is such that it purports to provide a means of compensatory redress, primarily for the benefit of creditors, against those who ‘misbehave’. In the case of disqualification, the state goes further and, by way of direct intervention, bars a delinquent individual from future directorial activity for a fixed period. The purpose of this thesis has, *inter alia,* been to assess the effectiveness of both public and private regulatory mechanisms in dealing with rogue directors of insolvent companies, with a special focus on improper trading and disqualification. The author has done so first by setting out the statutory basis and objectives for those mechanisms. These objectives in turn provided a platform upon which effectiveness could be determined. As the reader will have gathered, the outlook has not been particularly favourable. Indeed, the author has no trouble in concluding that each of the individual mechanisms discussed suffers its own considerable difficulties.

7.2 With that in mind, the author also went on to consider the impact of the SBEEA 2015 in this area. It is without doubt the most significant piece of legislation in the field of director liability since the inception of the IA 1986, perhaps with the sole exception being the introduction of undertakings pursuant to the IA 2000. The author was in part fortunate of it receiving Royal Assent during the process of researching and writing this thesis, though in other ways it has simply brought further uncertainties as to what the future holds in this area. As the reader will now be intimately aware, the author has thus sought to assess the *potential* implications of the Act upon the effectiveness of the enforcement mechanisms. Indeed, a substantial amount of time has been devoted to the subject. The author considered the implications of assignment upon the private enforcement regime in a discrete chapter, Chapter 5. Chapter 4 saw analysis of the extension of the *locus standi* of the improper trading liability provisions to administrators. And Chapters 2 and 3 dealt with, alongside some more minor matters, perhaps the most radical of them all: the implications of compensation orders and undertakings for the disqualification regime. In summary, whilst many of the changes are to be welcomed in principle, the author is truly sceptical of the potential impact of them at improving effectiveness overall.

7.3 For instance, the new ability of administrators being able to bring improper trading claims is most certainty a step forward. In fact, the author is of the view it is something so obvious that it ought to have been in place from the inception of the IA

1986, as was recommended by the Cork Committee. The law catching up with practice in this way will inevitably reduce costs and save time in circumstances where previously the administration would have been converted to a liquidation. This may have a marginal impact upon returns for creditors. It is, however, unlikely to increase the number of cases for the very reason that where an officeholder deemed proceedings to be desirable steps would have been taken so as to convert the administration, notwithstanding the additional cost and time involved in doing so.

7.4 In the case of the assignment of actions, the author has expressed a more troubled viewpoint. It has been argued in this thesis that giving officeholders the ability to assign claims was quite simply based upon the false premise that there is a funding crises in respect of commencing IA 1986 actions, in spite of the fact that no real empirical evidence to that effect has been presented. Whilst it is true that the LASPOA 2012 reforms have almost certainly been a blow to officeholders who might have previously been reliant upon the recovery of CFA uplifts and ATE premiums, there is no evidence empirical or otherwise to suggest an endemic funding crisis. Thus, in purporting to solve a problem that does not necessarily exist, the potential impact of the assignment provisions are muted. It has been gingerly suggested within this thesis that although assignment may come to outstrip the use of CFA/ATE agreements as the 'go to' means of commencing IA 1986 actions, it is unlikely to increase the overall number brought nor significantly enhance returns for creditors (except perhaps in cases at the lower end of the spectrum). This is predominantly due to the significant substantive legal hurdles, and issues of impecuniosity, faced by applicants neither of which assignment can assist with. However, this marginal benefit is obtained at the significant risk of creating a potential for a surge in nuisance or vexatious claims against directors. Many of whom could easily be pressured into early settlement, augmented by their own precarious financial positions, by companies the author terms 'insolvency trolls' on dubious grounds.

7.5 The potential harnessed within the compensation provisions are game-changing for creditors; at least on paper. However, as has been demonstrated, given the issues of director impecuniosity on the one hand, and the IS's self-imposed policy of 'cherry picking' particular cases to pursue for compensation on the other, the number of candidate directors will likely be very small indeed. Even smaller will be the number of successful cases. Therefore, ultimately, the author concludes that the provisions are unlikely to benefit creditors as considerably as the state has suggested. But, again, this approach comes at the expense of an increased scope for the oppression of directors by the SS. The author also has been highly critical of what appears to be currently a rather haphazard approach to dealing with circumstances in which compensation in the disqualification context and the improper trading mechanisms collide. If not properly managed, the not insignificant issues of double recovery and wasted litigation costs and time, as a result of simultaneous actions, might begin to rear their heads. Put simply, the compensation provisions strike the author as being a useful political tool – the successes will no doubt be few; but they will nonetheless be wheeled out by politicians at any opportunity as an indication of an overall effective regime.

FURTHER RESEARCH

7.6 One thing that struck the author in the process of writing this thesis is quite how little empirical research had been conducted in the area of director liability generally.

The present author has attempted to fill that lacuna in a modest way in the course of this thesis, notably in Chapter 3. Though, inevitably both financial and time constraints have had implications for what research could reasonably be carried out. Aside from the official disqualification statistics, and those collected by the state (and therefore obtainable pursuant to the FOIA 2000) staggeringly, and largely without exception, the empirical work in this field has been the work of comrades Hicks (historically) and Williams (more recently). Even in the recent *Transparency and Trust* consultation, the empirical justifications for a number of the SBEEA 2015 reforms are left entirely unclear. One of the difficulties that the author has identified, which in turn creates a danger, is that erroneous or outdated findings create a folklore in the insolvency community which, in turn, drives policy reform – perhaps in the wrong direction. To give but two examples, the author notes that the supposed funding difficulties with wrongful and fraudulent trading are still being ascribed to Hicks' now outdated study, which was limited in its sample size in any event. Moreover, the very *creation* of wrongful trading as a mechanism, and the expectations of academics and practitioners alike as to its performance, have been argued in this thesis to be based upon unproven and unevidenced assumptions (empirically or at all) by commentators. Indeed, this author has (albeit consciously) fallen into that very trap though, where possible, has sought to modernise the findings. It is hoped that in raising the matter at this juncture caution might be adopted in future by those that follow.

7.7 However, the real point to be made here is quite simply that more empirical analysis in this field is needed in order that policy can be shaped more accurately going forward. For instance, the author believes that considerable research into the economic consequences of limiting access to limited liability for owner managers is needed. Following that, more work needs to be done in relation to how best to do so, if it is deemed economically desirable. In the course of this thesis, in Chapter 6, the author has suggested that a system of education and training is one credible way forward. But, in truth, the merits of that approach cannot be stated with any certainty until more is known about the economic factors at play. Moreover, in a similar format to Hicks' study, a widespread survey of directors who have suffered enforcement action would be welcomed in this area, so that – if the regime is to be maintained in its current form – any impurities can be examined and eradicated. The prime opportunity for these investigations by the state, i.e. prior to the introduction of the SBEEA 2015, has unfortunately now come and gone. Given the political, economic, and legal uncertainties of modern times, following the UK's decision to depart the European Union – and the hierarchy of priorities that results from that – the chances of their being sufficient Parliamentary will to revisit this area in the short to medium term is, however, slim.

FINAL REMARKS

7.8 Given their nature as being *ex post facto* the enforcement mechanisms discussed herein will, by definition, be condemned to at least partial failure. This must be accepted as a truism. That is to say nothing of the other procedural and substantive legal difficulties that have been subject to analysis in this thesis. But, the approach of the state, it must be said, is fundamentally misdirected. At present, the policy focus remains firmly fixed in tempering the symptom and not the ultimate cause: uncontrolled access to limited liability. Of course, the state may do so rationally should it be shown that the economic benefits of the current position outweigh the cost of abuse. Yet, as has been expressed, the author is unaware of any evidence to support that proposition – particularly in the case of the owner-manager. Indeed, the approach of the state, evidenced by the passage of the SBEEA 2015, in continually *increasing* the scope of its regulatory machine might suggest that the inverse is true. Nonetheless, the state seems content to plough ahead with a regulatory regime of dubious efficacy, and with little promise of a *radical* shift in policy on the horizon. And so it goes.

BIBLIOGRAPHY

-- -- ‘Vince Cable proposes tougher rules for directors’ *BBC News* (15 July 2013) <http://bbc.in/2rGgX51> accessed 17 May 2016

-- -- *‘Catch Me If You Can paedophile Adam Hathaway jailed’ York Press* (9 January 2015) <http://bit.ly/1HBHN0d> accessed 28 February 2015

-- -- ‘Sir Philip Green's reputation 'still stained' despite BHS pension deal’, *BBC News* (1 March 2017) available at <http://bbc.in/2lborhw> accessed 30 August 2017

-- -- ‘BHS owner Dominic Chappell prosecuted by Pensions Regulator’, *The Telegraph* (22 August 2017) available at <http://bit.ly/2glLqRQ> accessed 30 August 2017

-- -- ‘Transparency and Trust Consultation Responses’ available at <http://bit.ly/2bM33GU> accessed 01 August 2016 (Warning: large file)

AHRQ, ‘Mixed Methods: Integrating Quantitative and Qualitative Data Collection and Analysis While Studying Patient-Centered Medical Home Models’ (PCMH Series, March 2013) available at <http://bit.ly/2fYMFcY> accessed 1 January 2017

Allain R, ‘The Traditional Lecture Is Dead – I Would Know I’m A Professor’ *Wired* (11 May 2017) <http://bit.ly/2pDzZs9> accessed 1 June 2017

Allen G, ‘Director Conduct Assessment Service’ Recovery (R3, Spring 2016) 38

Armour J, ‘Legal Capital: An Outdated Concept?’(2006) 7(1) EBOR 5

-- -- and Cumming DJ, ‘Bankruptcy Law and Entrepreneurship’, University of Cambridge ESRC Centre for Business Research (Working Paper No 300 March 2006)

Atkinson I, ‘Accuracy of data transfer: double data entry and estimating levels of error’ (2012) 21 Journal of Clinical Nursing 2730

Ayres I and Braithewaite J, *Responsive Regulation* (OUP 1992) 25

Bagnall V, ‘The compensation regime’ Recovery (R3, Winter 2016) 37

Bailey P, ‘Insolvency Service Consults on Insolvency Practitioner Fees and IP Regulation’ (2014) 349 SMCLN 1

Bainbridge SM and Henderson T, *Limited Liability: A Legal and Economic Analysis* (Edward Elgar 2016)

Baister S and Davies S, ‘Liability of Insolvency Practitioners for the Legal Costs of Litigation’ (May 2009) <http://bit.ly/2b21B3C> accessed 01 July 2016

Baldwin R, ‘The New Punitive Regulation’ (2004) 67 MLR 351

Ball J, ‘The deterrence concept in criminology and law’(1955) 46(3) J Crim LC & PS 346

Barchard K and Pace L, ‘Preventing human error: The impact of data entry methods on data accuracy and statistical results’ (2011) 27 Computers in Human Behavior 1834

Bardach E and Kagan RA, *The Problem of Regulatory Unreasonableness: Going by the Book* (Transaction Publishers 2010)

Beale HG (ed), *Chitty on Contracts: Volume 1* (32nd edn, Thomson Reuters 2015)

Belcher A, ‘What makes a director fit? An analysis of the workings of section 17 of the Company Directors Disqualification Act 1986’ (2012) Edin LR 386

Bennett SJ, ‘The Legal Aid, Sentencing and Punishment of Offenders Act 2012 (LASPO): One Year On, Final Report’ (A Bar Council Report, September 2014) available at <http://bit.ly/1vzRMwT> accessed 01 August 2016

Birks P, ‘Accessory Liability’ [1996] LMCLQ 1

Board of Trade, Report of the Company Law Amendment Committee (Cmd 2657, 1926)

Campbell A, ‘Wrongful Trading and Company Rescue’ (1994) 25 Cambrian LR 69

Carruthers BG and Halliday TC, Rescuing Business: The Making of Corporate Bankruptcy Law in England and the United States (OUP 1998)

Companies House, *Statistical Tables on Companies Registration Activities 2012-2013* (2013) <http://bit.ly/ 2pTlhBq> accessed 14 April 2017

-- -- *Companies Register Activities 2015-2016* (2016) <http://bit.ly/2pTlhBq> accessed 14 April 2017

-- -- *Companies Register Activity in the United Kingdom 2016-2017* (2017) <http://bit.ly/2vbSQg2> accessed 1 August 2017

-- -- ‘Events Calendar’ available at <http://bit.ly/2wV6SYu> accessed 20 February 2017

-- -- ‘First Time Director Seminar’ <http://bit.ly/2t0mLrW> accessed 1 May 2017

Cheffins B, *Company Law: Theory Structure and Operation* (Clarendon Press 1997)

Chen W, ‘Abolition of legal capital requirements under Chinese Company Law 2014 and its potential influence: a comparative study in selected countries’ (2014) 35(12) Co Law 371

Chesterman M, *Small Businesses* (Sweet & Maxwell, 1972)

Cook C, ‘Wrongful trading – is it a real threat to directors or a paper tiger?’ (1999) 3(Apr) Insolv L 99

Crinson K and Morphet S, ‘Funding for actions brought by insolvency officeholders’ (2011) 24(7) Insolv Int 108

Danks M, ‘The engine that drives director conduct reporting’ Recovery (R3, Autumn 2016) 13

Davies P, *Accessory Liability* (Hart 2015)

Denning A, HL Deb 1 April 1985, vol 462, col 40

Department for Business, Energy and Industrial Strategy Committee, *Corporate governance: Third report of session 2016-17* (HC 2016-17, 702)

Department for Business, Innovation and Skills Committee, *The Insolvency Service: Sixth Report of Session 2012-13* (HC 2012-13, 675)

Department for Business, Innovation and Skills, 'Transparency and Trust: Enhancing the Transparency of UK Company Ownership and Increasing Trust in UK Business – Discussion Paper' (July 2013) <http://bit.ly/1F8U9Ks> accessed 18 October 2015

-- -- 'Consultation Outcome – Company ownership: transparency and trust discussion paper' (15 July 2013) available at <http://bit.ly/1nD5QSo> accessed 1 August 2016

-- -- 'Impact Assessment - Changes to reporting on the conduct of directors by insolvency office-holders. Red Tape Challenge Measure' (2014) available at <http://bit.ly/2vM8A9F> accessed 14 April 2017

-- -- 'Impact Assessment – Extending the time limit for director disqualification proceedings under the CDDA' (2014) available at <http://bit.ly/2elSFZn> accessed 14 April 2017

-- -- 'Impact Assessment – Giving the court and Secretary of State (SoS) a power to make a compensatory award against a director' (2014) available at <http://bit.ly/2esCrRH> accessed 14 April 2017

-- -- 'Impact Assessment: Enabling Liquidators and Administrators to assign to third parties certain rights of action that only they can bring under the Insolvency Act 1986 and to extend to the right to bring fraudulent and wrongful trading actions to an administrator' (BIS INSS007) available at <http://bit.ly/2c2UtnE> accessed 01 August 2016

-- -- 'Impact Assessment: Matters to be taken into account by the Court when determining that a person is unfit to act as a company director' (2014) at <http://bit.ly/2uVywQ8> accessed 1 July 2017

-- -- 'Transparency and Trust: Enhancing the Transparency of UK Company Ownership and Increasing Trust in UK Business – Government Response' (April 2014) <http://bit.ly/1no7pXg> accessed 01 August 2016

De Geest G, 'Hoe maken we van de rechtswetenschap een volwaardige wetenschap' (2004) Nederlands Juristenblad 58

Department for Transport, 'Effective Interventions for Speeding Motorists' (2006) available at <http://bit.ly/2tkw2x5> accessed 1 June 2017

Diamond AL, 'Corporate Personality and Limited Liability' in Orhnial, Tony (ed), *Limited Liability and the Corporation* (Croom Helm 1982)

Dine J, 'Punishing directors' (1994) JBL 325

Djanogly J, HC Deb 24 May 2012, col 94W

Department for Trade and Industry, *Report of the Company Law Committee* (Cmnd 1749, 1962)

-- -- *Company Law Reform* (Whitepaper, Cmnd 5391, 1973)

-- -- *Insolvency Law and Practice: Report of the Review Committee* (Cmnd 8558, 1982) (Cork Report)

-- -- *Modernising Company Law* (White Paper, Cm 5553, 2002)

-- -- *Company Law Reform* (Cm 6456, 2005)

-- -- *A Revised Framework for Insolvency Law* (Whitepaper, Cmnd 9175, 1984)

Doyle L, 'Anomalies in the wrongful trading provisions' (1992) 13(5) Co Law 96

Easterbrook FH and Fischel DR, *The Economic Structure of Corporate Law* (Harvard University Press 1991)

Fakih KM, 'The one-member company: a comparison study of the one-member company in France, Europe, United States and Lebanon' (2014) 25(6) ICCLR 221

Farrar J, 'Fraudulent trading' [1980] JBL 336

-- -- Furey N, and Hannigan B, *Farrar's Company Law* (3rd edn, Butterworths 1998)

Finch V, 'Disqualification of Directors: A Plea for Competence' (1990) 53 MLR 385

-- -- 'Company Directors: Who Cares About Skill and Care?' (1992) 55(2) MLR 179

-- -- 'Disqualifying Directors: Issues of Rights, Privileges and Employment' (1993) 22(1) ILJ 35

Fletcher A, HC Deb 05 June 1985, vol 80, col 178W

Fletcher AJ, HC Deb 24 May 2012, col 94W

Fletcher I, *The Law of Insolvency* (4th edn, Sweet & Maxwell 2009)

Freedman J and Godwin M, 'Incorporating the micro business: perceptions and misperceptions' in Hughes A and Storey DJ (eds), *Finance and the Small Firm* (Routledge 1994)

Garvey S and Others, *Encyclopedia of Banking Law* (LexisNexis UK 1996)

Gilbert WS and Sullivan A, 'Mr Goldbury' from the opera *Utopia Limited* (1893). The full libretto is available at <http://bit.ly/2q15iNm> accessed 15 May 2017

Gov.UK, 'Learning to Drive' <http://bit.ly/2s23fKa> accessed 1 June 2017

Griffin S, 'Accelerating disqualification under section 10 of the Company directors disqualification act 1986' 2002 2(Mar) IL&P 32

Halpern P, Trebilcock M and Turnbull S, 'An Economic Analysis of Limited Liability in Corporation Law' (1980) UTLJ 30 117

Henry D 'Disqualification of Directors: A View from the Inside' in Rajak H (ed) *Insolvency Law: Theory and Practice* (1993 Sweet & Maxwell)

Hicks A, 'Wrongful trading – has it been a failure?' (1993) 8(5) IL&P 134

-- -- *Disqualification of Directors: No Hiding Place for the Unfit?* (ACCA Research Report 59, 1998)

-- -- 'Director disqualification - is it a lottery?' (1999) 15(3) IL&P 73

-- -- 'Director disqualification - the National Audit Office follows up' (1999) 15(4) IL&P 112

-- -- 'Director disqualification: can it deliver?' (2001) JBL 433

Houghton S, 'Interview with Philip King' Recovery (R3, Spring 2012) 46

Impey D and Montague N, *Running a Limited Company* (Jordans 1990)

Information Commissioners Office, 'Data Protection Principles' available at <http://bit.ly/1E2lQ8V> accessed 10 July 2017

Institute of Directors, 'Professional Development of and for the Board' (January 1990)

-- -- 'Chartered Director' <http://bit.ly/2toupz1> accessed 1 January 2017

-- -- 'Training' <http://bit.ly/2tkn3Mm> accessed 1 January 2017

Insolvency Service, *Business Confidence Stakeholder Satisfaction Survey 2009: Management Summary* (2009) [Source Unavailable]

-- -- *Annual Report and Accounts 2011-2012* (2012) <http://bit.ly/2tsQOdx> accessed 30 April 2016

-- -- *Stakeholder Confidence Survey 2012* (2013) available at <http://bit.ly/2iJGZEL> accessed 1 April 2017

-- -- *Annual Report and Accounts 2012-2013* (2013) <http://bit.ly/1qxxDFF> accessed 30 April 2014

-- -- *Supporting Data for Comparison of Performance in 2012-2013 to Previous Years* (2013) <http://bit.ly/1iNa5YC> accessed 14 April 2014

-- -- 'Red Tape Challenge - changes to insolvency law to reduce unnecessary regulation and simplify procedures: Consultation' (2013) available at <http://bit.ly/2x9eBRW> accessed 14 April 2017

-- -- 'Guide to Insolvency Service Enforcement Outcomes' (2015) <http://bit.ly/2tXg6Rx> accessed 1 June 2017

-- -- *Annual Report and Accounts 2015-16* (2016) <http://bit.ly/2tXPfF9> accessed 1 July 2017

-- -- *Stakeholder Confidence Research: Executive Summary 2015-2016* (2016) available at <http://bit.ly/2eschi1> accessed 1 April 2017

-- -- 'Company Directors Disqualification Act 1986: Interim Guidance Notes for the use of the Director Conduct Reporting Service' (2016) available at <http://bit.ly/2wkPavS> accessed 10 August 2017

-- -- *Insolvency Service Enforcement Outcomes 2016-17* (2017) <http://bit.ly/2u35zoP> accessed 1 July 2017

-- -- 'Disqualified Directors Search' <http://bit.ly/1eEx9GH> accessed 14 April 2014

-- -- 'Investigations and Enforcement Services Breach Questionnaire' <http://bit.ly/2tsEg5Z> accessed 1 July 2017

-- -- Disqualification Outcomes Facility <http://bit.ly/2u2VWq7> accessed 14 April 2014

Jackson H and Roe M, 'Public and Private Enforcement of Securities Laws: Resource-Based Evidence' (2009) 93 JFE 207

Jackson LJ, 'The Civil Justice Reforms and Whether Insolvency Litigation Should Be Exempt' (The Mustill Lecture, Leeds, 16 October 2015) available at <http://bit.ly/1RRLHap> accessed 01 August 2016

-- -- (ed), *Civil Procedure: The White Book Service 2016* (Sweet & Maxwell, 2016

Jensen MC and Meckling WH, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3 JFE 305

Kahn-Freund O, 'Some Reflections on Company Law Reform' (1944) 7 MLR 54

Keay A, Company Directors' Responsibilities to Creditors (Routledge-Cavendish 2007)

-- -- 'The Public Enforcement of Directors' Duties: A Normative Inquiry' (2014) 43 CLWR 89

Kempin FG, 'Limited Liability in Historical Perspective' (1960) 4(1) ABLA Bulletin 32

Leebron DW, 'Limited Liability, Tort Victims and Creditors' (1991) Colum LRev 1565

Lilly D, Davies N and Chinnery A, 'Transparency & Trust: a new era for directors' disqualification?' (2014) available at <http://bit.ly/2eHwFbF> accessed 4 February 2017

Loughrey J, 'Smoke and mirrors? Disqualification, accountability and market trust' (2015) 9(1) LFMR 50

Manolete Partners Plc, 'Frequently Asked Questions' <http://bit.ly/2bQMSdl> accessed 01 August 2016

-- -- 'Newsletter Autumn 2015' available at <http://bit.ly/2bIyOpp> accessed 01 August 2016

-- -- 'R3 Survey shows the majority of IPs who use litigation funding use Manolete Partners' available at <http://bit.ly/2cjHqPg> accessed 01 August 2016

Mason R, 'Vince Cable To Bring In Tougher Penalties For 'Dodgy Directors' *The Guardian* (19 April 2014) <http://bit.ly/2q6crfL> accessed 17 May 2016

McCormack G, *Corporate Rescue Law – an Anglo-American Perspective* (Edward Elgar 2008)

Meston J, HL Deb 15 January 1985, vol 458, col 915

Meyer C, *Firm Commitment: Why the corporation is failing us and how to restore trust in it* (Oxford University Press 2013)

Milman D, 'Partial disqualification orders' (1991) 12 Co Law 224

-- -- 'The 'phoenix syndrome'' (2001) 6 Insolv L 199

-- -- 'Two cases of interest for company directors operating in the twilight zone' (2008) 21(2) Insolv Int 25

-- -- *Governance of Distressed Firms* (Edward Elgar 2013)

Mirrlees-Black C, *Disqualification from Driving: An Effective Penalty?* (Home Office Research and Planning Unit, Paper 74, 1993)

Mithani A, *Mithani: Directors' Disqualification* (1998 LexisNexis)

Mokal R, 'An Agency Cost Analysis of the Wrongful Trading Provisions: Redistribution, Perverse Incentives and the Creditors' Bargain' (2000) 59(2) CLJ 335

Möser K, 'Restrictions after personal insolvency' (2013) JBL 679

Moss G, 'No compensation for wrongful trading – where did it all go wrong?' (2017) 30(4) Insolv Int 49

National Audit Office, *Report by the Comptroller and Auditor General: The Insolvency Service Executive Agency, Company Director Disqualification* (HC 1992-1993, 907)

-- -- *Report by the Comptroller and Auditor General: Insolvency Service Executive Agency, Company Director Disqualification – A Follow Up Report* (HC 1998-1999, 424)

National Fraud Authority, 'Annual Fraud Indicator 2013' (June 2013) <http://bit.ly/1zU4oQI> accessed 01 January 2016

Ng CK, Smith JK and Smith RL, 'Evidence on the Determinants of Trade Credit Terms in Interfirm Trade' (1999) 54 J Fin 1109

Oakley D and Warrell H, 'UK to crack down on negligent directors' *Financial Times* (14 July 2013) <http://on.ft.com/2vtPmGY> accessed 17 May 2016

Oditah F, 'Wrongful trading' [1990] LMCLQ 205

Public Accounts Committee, 18th Report (HC 1993-1994, 167)

Paterson S, 'Compensation orders: a quiet revolution' Recovery (R3, Summer 2017) 32

Posner R, 'The Rights of Creditors of Affiliated Corporations' (1967) 43 U Chi L Rev 499

Prentice DD, 'Corporate Personality, Limited Liability and the Protection of Creditors' in Grantham R and Rickett C (eds), *Corporate Personality in the Twentieth Century* (Hart Publishing 1998)

R3, 'Directors Disqualification: Room for Improvement' (2011) <http://bit.ly/2tXkQ9Y> accessed 1 January 2017

-- -- 'The Fraud Landscape: Insolvency and the fight against fraud' (January 2015) <http://bit.ly/17dWJ7L> accessed 01 January 2016

Raab D, HC Deb 17 December 2015, col 420W

Rajak H, 'The complex story of wrongful trading' (2017) 392 Co LN 1

Richardson BJ and Sjåfjell B (eds), *Company Law and Sustainability: Legal Barriers and Opportunities* (Cambridge University Press 2015)

Shine P, 'Dishonesty in civil commercial claims: a state of mind or a course of conduct?' [2012] 1 JBL 29

Smith A, *An Inquiry into the Nature and Causes of the Wealth of Nations* (MetaLibri Digital Edition 2007)

Taylor B, 'Wrongful trading' Recovery (R3, Spring 2015) 16

Taylor E and Shepherd J, 'Recent developments affecting directors' (2016) 29(3) Insolv Int 42

The Complete University Guide, 'MBA' <http://bit.ly/2tXQYrw> accessed 1 May 2017

The Stationary Office, 'Review of Civil Litigation Costs: Final Report' (December 2009) available at <http://bit.ly/1IkgolZ> accessed 01 August 2016

Van Hoecke M, 'Legal Doctrine: Which Method(s) for What Kind of Discipline?' in Van Hoecke M (ed), *Methodologies of Legal Research: Which Kind of Method for What Kind of Discipline?* (Hart Publishing 2011)

Von Hirsch A and Wasik M, 'Civil Disqualifications Attending Conviction: A Suggested Conceptual Framework' (1997) 56(3) CLJ 599

Walters A and Davis-White M, *Directors' Disqualification & Insolvency Restrictions* (3rd edn, Sweet & Maxwell 2010)

Walters W, 'Enforcing Wrongful Trading – Substantive Problems and Practical Disincentives' in Rider B (ed), *The Corporate Dimension* (Jordans Publishing 1998)

Walton P, 'The Likely Effect of the Jackson Reforms – an Empirical Investigation' (An R3 Report, April 2014) <http://bit.ly/2atR1qh> accessed 1 July 2016

-- -- 'Insolvency litigation - a case of 'if it ain't broke, don't fix it?'' (2015) Insolv Int 9

-- -- 'Insolvency Litigation and the Jackson Reforms – An Update' (An R3 Report, April 2016) <http://bit.ly/1SO0cLE> accessed 01 July 2016

Wikipedia, 'Mike Ashley (businessman)' available at <http://bit.ly/2vHxEiU> accessed 1 January 2016

Willcock J, '4,000 Rogue Directors on Loose in UK Companies' *The Independent* (28 October 1996) at <http://ind.pn/2uCfcrO> accessed 3 January 2015

Williams C and McGee A, *A Company Director's Liability for Wrongful Trading* (ACCA Research Report No. 30, 1992)

Williams K, 'Public knowledge of statutory penalties: the extent and basis of accurate perception' (1980) 23(1) The Pacific Sociological Review 105

Williams R, 'Disqualifying Directors: A Remedy Worse than the Disease?' (2007) 7(2) JCLS 213, 235-236

-- -- *Disqualification Undertakings: Law, Policy and Practice* (Jordans Publishing Limited 2011)

-- -- 'Civil Recovery from Delinquent Directors' (2015) 15(2) JCLS 311

-- -- 'What Can We Expect to Gain from Reforming the Insolvent Trading Remedy?' (2015) 78(1) MLR 55

Wormser M, *Frankenstein, Incorporated* (McGraw-Hill Book Company 1931)