

Improving the law on director liability in distressed companies

Professor David Milman, Dr Sofia Ellina, Dr John Wood

Policy Context

The current regime of insolvency laws and processes fails to deal with company directors in a convincing manner due to ambiguity, lack of coordination, and difficulties in enforcement.

The main rules governing the liability of directors in cases of corporate insolvency can be found both in the common law and in statutory provisions. Statutory duties and liabilities imposed on directors can be found in the Companies Act 2006, the Company Directors Disqualification Act 1986, and the Insolvency Act 1986.

Key research findings

Directors are treated inconsistently. Sometimes they are seen as competent individuals with rights to direct limited liability companies worthy of strong protection. At other times they are seen as fortunate individuals who exercise the privilege of directing companies, and who should not be surprised if they lose those privileges to protect the public or raise standards.

- **Differences in the perception of directors by the judiciary may lead to varied enforcement.**
- **Clear standards and guidelines are needed to balance the rights and responsibilities of directors more effectively,** promoting a regulatory environment and judicial understanding that supports both business innovation and public interest protection.
- **Directors are increasingly exposed to legal risk** due to the ambiguity of the duties of directors and varied interpretations of the rules governing them.

- **Some directors feel that they are treated unfairly by the rules governing their liability.** The varied perception by the judiciary of how those rules should be interpreted and applied may contribute to this. If the judiciary were consistent in their attitudes, this would be fairer to directors.
- **The current state of wrongful trading creates uncertainty and may discourage directors from taking reasonable risks,** potentially hindering entrepreneurial activity and harming the company's prospects for rescue.
- **The provisions governing the liability of directors are too severe and provide only blunt, inefficient tools.** For example, wrongful trading provisions in 214 and 246ZB, Insolvency Act 1986 state that where a company is in liquidation (or administration) a liquidator (or administrator) can apply to have a director declared personally liable to contribute to company assets. Judges may use these provisions to punish directors whose actions are seen as commercially immoral.

Policy recommendations

- **Policymakers should promote ongoing legal education and awareness of evolving duties** so that directors are supported in managing increasing risks.
- **Insolvency procedures should be designed to encourage capable individuals to accept directorships** and to apply their expertise during periods of corporate distress, rather than deter them.
- **Draw on academic research, such as that conducted at Lancaster University Law School**, to inform policy development and enhance understanding in this area.
- **Enhance regulation by introducing more effective control, particularly through stricter checks on prospective directors.** Until policymakers challenge the ease with which individuals can become directors, the problems of policing limited liability companies and those who manage them will persist.
- **Legislation should remove practical impediments to enforcement, particularly those that undermine fairness.** Rather than introducing a blueprint set of rules in statutory form, reform should focus on eliminating impediments such as the high cost and limited availability of litigation funding, procedural complexity, and unequal access to legal advice. Addressing these obstacles would improve access to justice and support fairer outcomes in corporate and insolvency contexts.
- **The statutory framework should enable the courts to use their judgement to produce and apply rules that are commercially operable and consistent.**

Work with us

For a recent example of research in this area, see the forthcoming Oxford University Press edited volume by Dr John Wood, Dr Sofia Ellina, and Dr John Tribe (University of Liverpool) titled; *Directors and Creditors: Law and Liability*.

Professor David Milman

is Professor Emeritus at Lancaster University. He is an expert on Corporate Law and Insolvency Law.

Contact Prof Milman at d.milman@Lancaster.ac.uk

Dr Sofia Ellina

is a Lecturer in Law at Lancaster University. Her main research interests are in the fields of insolvency law and financial law.

Contact Dr Ellina at s.ellina@Lancaster.ac.uk

Dr John Wood

is a Lecturer in Company and Insolvency Law at Lancaster University. His research interests are focused on company and corporate insolvency law issues.

Contact Dr Wood at j.m.wood@Lancaster.ac.uk