Directors Lacking Direction

Critiquing the Framework of Directors' Duties as it Currently Stands Under the Companies Act 1993

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I Introduction

Directors have enormous sway over the success or failure of companies. Their actions can result in significant profits or losses for many interested parties. As such, these actions must adhere to certain standards of practice, to ensure that they neither abuse their position nor frivolously deal with the assets of others. This is the principle which has resulted in the creation and enforcement of directors' duties. These duties are owed to the company and are enforceable through several different avenues. The duties, for the most part, developed through case law. The Companies Act 1955 held no mention of duties generally, although did disallow the practice of fraudulent trading. Upon reviewing company law as it stood under this Act, the Law Commission found that "the present law relating to the duties of directors is inaccessible, unclear and extremely difficult to enforce." This resulted in propositions for reform, and the eventual incorporation and codification of directors' duties in the Companies Act 1993.

The result of this attempted simplification of the law relating to these duties has not been as intended. Situations of insolvency have become particularly problematic. In such cases there has arisen a tendency to plead a breach of every duty in the hope that at least one is successful. This dissertation focuses on cases where creditors make such claims. It has become clear through many cases both that the law lends itself to over pleading, and that directors' duties have become muddled when applying them to situations of breach.

Part 1 of outlines the current statutory regime for enforcing directors' duties. This dissertation focuses on four of these duties; sections 131, 135, 136 and 137. Part 2 considers proposals made by the Law Commission before the current statute was drafted, and observes how these proposals were adopted or changed in the Act. Part 3 reviews the judicial authorities which have arisen over nearly 30 years of case law. Part 4 focuses on how courts have applied directors' duties, particularly the High Court, in an attempt to discern if the lack of clarity identified by the Law Commission remains. Part 5 briefly reviews the equivalent UK law, with a primary focus on noting the consequences of codifying directors' duties. The final part provides a critique of the law as it stands.

II The Companies Act 1993

A Overview

The law of directors' duties is governed by the Companies Act 1993. Sections 131-138B of the Act outline the duties owed by directors to companies. These sections were intended to codify duties which had developed through case law, as well as much of the Companies Act 1955. The development of duties owed by directors to companies occurred through two branches of the law – the common law and the law of equity. Common law duties fit broadly into the class 'duties of care'. These duties have evolved with the law of torts, notably through the development of negligence as a cause of action. Equitable duties fall into the category of 'duties of loyalty'.[1]

While the duties owed by directors are now of a statutory nature, this historical development remains relevant. This is because the statute does not provide full answers on how to approach causation when applying the duties, nor does it offer any assistance on issuing remedies (other than providing an avenue for remedies to be ordered, at the discretion of the Court). Courts have therefore looked to the origins of each duty when enforcing a breach, as the historical causation tests and remedies applied in the case law remain the appropriate ways of enforcing these duties.[2]

Equitable duties will allow for recovery through two primary means: an account of profits and equitable compensation.[3] Each is appropriate in different circumstances, and causation tests will attach according to which remedy is sought. Duties of care lead to claims for damages, applied in a common law fashion. Causation will involve questions of foreseeability and other related common law principles.

This dissertation focuses on the law of directors' duties as they relate to creditors. While these duties are owed to the company, it has been accepted that in times of insolvency, and even in times of near insolvency, directors must consider the interests of creditors.[4] This recognises the fact that it is creditors who primarily bear the loss when a company reaches the point of insolvency.

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[1] Gordon Walker, Alma Pekmezovic, Pamela Hanrahan, Ian Ramsay and Geof Stapledon *Commercial Applications of Company Law in New Zealand* (5th ed, CCH New Zealand Ltd, 2015) at 255
[2] *FXHT Fund Managers Ltd (in liq) v Oberholster* [2010] NZCA
[3] *Sojourner v Robb* [2008] 1 NZLR 751
[4] *Nicholson v Permakraft (NZ) Ltd* [1985] 1 NZLR 242

B Section 131

Section 131 imposes a duty on directors to act in good faith and in what the director believes to be the best interests of the company.[5] This duty developed from the equitable notion that a fiduciary must not use their position in a way which is detrimental to the party on whose behalf they are acting.[6] This idea began with the decision of *Re Smith v Fawcett*, which stated that directors must act in the best interests of the company and not for any collateral purpose.[7] The duty subsequently developed through the Courts of equity and maintains its fiduciary nature even in statutory form.[8]

The wording of the section clearly indicates that the test is subjective in nature from the point of view of the director in question, as it states "what the director believes to be int eh best interests of the company".[9] However, in applying the duty, Courts have imposed the requirement that the belief of a director must be reasonably held.[10]

The origins of this duty become relevant when considering remedies available and causation tests in pursuing breaches of directors' duties. Due to the equitable nature and development of the duty, equitable remedies will be available for breaches of s 131, as seen in *Hedley v Albany Power Centre*.[11] These duties may take the form of an account of profits or equitable compensation.[12] Which of these is being pursued will determine the appropriate test for causation.

C Sections 135/136

Section 135, entitled reckless trading, requires directors not to enter into business arrangements which are "likely to create a substantial risk of serious loss to the company's creditors".[13] This duty is designed to protect creditors, but is owed to the company as a whole rather than any particular creditor.

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[5] Companies Act 1993, s 131(1)
[6] Derek French, Stephen Mayson & Christopher Ryan *Company Law* (33rd ed, Oxford University Press, Oxford, 2016) at 478
[7] *Re Smith v Fawcett Ltd* [1942] Ch 304 (CA)
[8] *Sojourner v Robb*, above n 3
[9] Companies Act 1993, s 131(1)
[10] Susan Watson "Duties of Directors: Duties of Honesty and Loyalty" in Company and Security Law in New Zealand (Brookers Ltd, Wellington, 2008) at 337
[11] *Hedley v Albany Power Centre Ltd (in liq)* (2006) 2 NZCCLR 1148
[12] At [31]
[13] Companies Act 1993, s 135

Mainzeal is a case which offers a detailed application of s 136, and importantly distinguishes between sections 135 and 136 at length.[14] The distinction articulated is that where s 135 assesses risk taking, s 136 focuses not on risks but on "the performance of specific obligations and the associated beliefs of the directors".[15] To establish a breach, it must be shown that a director believed the company would not be able to meet its obligation at the time of committing to the obligation.[16] This criteria is also satisfied where a director believed that the obligation would be met, but this belief was unreasonably held. Application of this section therefore involves an objective assessment of the director's beliefs, rather than their actions.[17]

Sections 135 and 136, which are concerned with unreasonably incurring the risk of insolvency, differ from the other statutory duties in their historical development. Where the other duties were pooled from common law and equity, these provisions are derived from s 320 in the Companies Act 1955.[18] This section targeted fraudulent trading – an offence directed at remedying clear wrongdoing. This differs from the other duties which developed through case law, as negligence type breaches as well as breaches of fiduciary duties are more concerned with remedying the breach than punishing the director. Section 135 particularly seems to lie somewhere between these two purposes, although I argue that it should remain purely compensatory, rather than punitive.

In *FXHT Fund Managers*, the Court of Appeal held that a breach of s 135 is essentially a failure to exercise reasonable care in the particular circumstances.[19] This suggests that it is a duty of care similar to s 137, which may be relevant for an assessment of remedies.

These duties are inherently the most problematic both to draft and to apply. This is because risks are an essential part of business, and balancing the right to take business risks against the duty to do so responsibly is a difficult task.[20] It is particularly difficult to assess this where a company is insolvent, as in essentially all ss 135 and 136 cases, as Courts must attempt to

[14] *Mainzeal Property and Construction Ltd (in liq) v Yan* [2019] NZHC 255
[15] At [297]
[16] Companies Act, s 136
[17] *Mainzeal v Yan,* above n 16, at 298
[18] Companies Act 1955, s 320
[19] *FXHT Fund Managers Ltd (in liq) v Oberholster*, above n 2, at [30]
[20] Hon Justice Tompkins "The Stace Hammond Grace Lecture in Commercial Law. Directing the Directors: The Duties of Directors Under the Companies Act 1993" (Waikato University)

disregard hindsight and place themselves in the shoes of directors at the time of the decision making.[21]

The result Supreme Court decision of *Debut Homes v Cooper* makes it clear that ss 135 and 136 are not fiduciary in nature, and are statutory duties only.[22]

D Section 137

Section 137 imposes a duty of care on directors.[23] This duty can trace its origins to both equity and the common law, although it has primarily developed through the common law tort of negligence.[24] The section states that directors "must exercise the care, diligence and skill that a reasonable director would exercise in the same circumstances," and outlines some factors for Courts to consider in assessing this.[25]

The duty of care primarily attracts an objective assessment, however there is also a subjective element to the section's interpretation.[26] This comes from the reference in to the position of the specific director in question and the nature of the responsibilities undertaken by him or her.[27] One reason for the inclusion of this in the section is to allow for differing standards of care for those in specialist positions. Peter Watts suggests that this is intended to create an increased degree of scrutiny in certain cases, rather than to generally introduce a sliding scale of care required by directors.[28]

1 Sections 135/136 compared with s 137

Sections 135 and 136 to some degree resemble duties of care, as they address foreseeability of loss and s 136 requires an assessment of reasonableness, as does s 137. Despite this, they are intended to remedy different situations. Sections 135 and 136 are primarily concerned with insolvency scenarios.[29] While they can be applied before insolvency is a real concern, this is unlikely to happen. This is because the evidential burden of proving a risk of insolvency is difficult to achieve when a company is not in financial difficulty – either nearing insolvency or already at this point. This purpose is evidenced in the Law Commission

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[21] Watts, Campbell and Hare *Company Law in New Zealand* (LexisNexis, Wellington, 2011) at 559
[22] *Cooper v Debut Homes* [2020] NZSC 100 at [159]
[23] Companies Act 1993, s 137
[24] John Farrar "Duties of Directors: Duties of Honesty and Loyalty" in *Company and Security Law in New Zealand* (Brookers Ltd, Wellington, 2008) at 386
[25] Companies Act 1993, s 137
[26] Watts, Campbell and Hare *Company Law in New Zealand*, above n 23, at 554
[27] Section 137(c)
[28] Peter Watts *Directors' Powers and Duties* (LexisNexis, Wellington, 2009) at 241
[29] At 267

proposal of a section entitled "Solvency", which was essentially split into these two sections in the resultant statute.[30]

Section 137, by contrast, is generally applicable when shareholders or creditors are unhappy with the conduct of a company's directors. These sections will overlap where insolvency is a concern, however s 137 is generally more widely applicable. Section 137 looks at a director personally, as opposed to the conduct they have committed the company to. This will encompass directors who are caught doing nothing, as well as those engaging in inappropriate conduct.

It is important to identify the conduct which each duty looks to monitor in order to recognise where courts have strayed from this purpose.

E Section 301

Section 301 is an enforcement provision, which allows certain parties to receive remedies for breaches of directors' duties.[31] Shareholders have other avenues available for remedying such breaches, for example through a derivative action or prejudiced shareholder action,[32] however for creditors s 301 is the only method for such a claim outside of liquidator proceedings, which are engaged in by liquidators rather than creditors. The Court of Appeal in *Sojourner* described the section as "a procedural short cut by which a liquidator, creditor or shareholder may pursue claims which a company in liquidation may have against, inter alia, its former directors."[33] The power given by this section to the Courts in relation to a breach of duty is to order the director in breach to:

a) inquire into the conduct of the director; and
b) order that person –
    i) to repay or restore the money or property or any part of it with interests at a rate the court thinks just; or
    ii) to contribute such sum to the assets of the company by way of compensation as the court thinks just [34]

[30] Law Commission *The Draft Companies Act* (NZLC R9, 1989) s 105
[31] Companies Act 1993, s 301
[32] Sections 167 and 174
[33] *Sojourner v Robb* [2008] 1 NZLR 751 above n 3, at [53]
[34] Companies Act s 301

Section 301(1)(c) clarifies that where the application is made by a creditor, the Court may order that money or property be transferred to the creditor.[35] This raises the question of how literally this is to be interpreted. In situations of liquidation, funds are likely to be limited. Allowing individual creditors to make claims in priority over the general creditor pool would be directly contrary to the general law of liquidation. *Mitchell v Hesketh* clarified the position early in the life of the Companies Act 1993, stating that "a creditor cannot rely upon s 301(1)(c) to recover from a director in the second circumstance where the director has been guilty of negligence, default or breach of duty or trust".[36] There may some exceptions where individual creditors can receive awards directly, but this dissertation need not focus on this. Which creditors receive the benefits of a successful award is not so important as how quantum is determined for the purposes of this discussion.

As was well articulated in *Willburn Furniture*, the application of s 301 involves a two-stage approach.[37] This firstly involves an assessment of whether there has been a breach of duty. If this is shown to be the case, courts will ask to what extent directors should contribute to the losses of the company.[38] The correct way of applying this second limb of the approach is to ascribe the appropriate causation test to match the duty breached.[39]

Importantly and obviously, directors cannot claim more under s 301 than they can claim through standard liquidation processes.[40] This becomes particularly relevant where multiple breaches are found, as often only one breached duty is necessary to consider (in terms of causation and the remedies available) to reach this full amount.

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[35] Section 301(1)(c)
[36] *Mitchell v Hesketh* (1998) 8 NZCLC 261,559
[37] *Willburn Furniture and Restorations Ltd (in liq) v Gledhill* [2016] NZHC 331 at [47]
[38] At [65]
[39] *FXHT Fund Managers Ltd (in liq) v Oberholster*, above n 23, at [28]
[40] *Sojourner v Robb,* above n 3, at [54]

III Law Commission Proposals

Before the 1993 Act was created, reform of company law was considered at length. The law at the time comprised the Companies Act 1955 as well as a large array of case law. The Law Commission issued several reports discussing potential reform through which they outlined what they considered to be a desirable company law schematic, culminating in a 1989 report[41] and accompanying draft Act.[42] This work was then added to and amended by the Law Reform Division.[43] As a result, the 1993 Act incorporates some of the Law Commission's proposals while disregarding or changing others.

The Law Commission's view was that the law of directors' duties before the 1993 Act, which was discerned from extensive case law, was "inaccessible, unclear and extremely difficult to enforce." [44] They aimed to find a system of accountability which was both relatively easy for directors to understand and straightforward for courts to apply.[45]

A Hierarchy of duties

The Law Commission's report proposed codifying a large array of duties from case law.[46] However, to maintain a broad range of duties means that potential clashes are difficult to avoid. Duties might be played off against one another by clever litigators, for example by suggesting that acting in the company's best interests is contrary to another duty. To resolve this the Law Commission proposed a hierarchy of duties.[47] This hierarchy established a fundamental duty to "act in good faith and in a manner that he or she believes on reasonable grounds is in the best interests of the company".[48] All other duties and interests would only be applied and considered if doing so was consistent with the fundamental duty. It follows from promoting one duty above all others that this fundamental duty could also provide a defence for breaches of other duties, for example if a director acted unreasonably but in the best interests of the company.

[41] Law Commission *Company Law: Reform and Restatement* (NZLC R9, 1989)
[42] Law Commission (R9), above n 32
[43] Hon Justice Tompkins "The Stace Hammond Grace Lecture in Commercial Law. Directing the Directors: The Duties of Directors Under the Companies Act 1993" (Waikato University)
[44] Law Commission (R9), above n 43, at [184]
[45] At [186]
[46] At [186]
[47] At [194]
[48] Law Commission (R9), above n 32, s 101

A fundamental duty would be beneficial to both Courts and directors. The utility to the Courts in applying multiple duties is obvious. As discussed above, where several duties are breached it is easier to know which one takes precedence, and this could lead to more consistency in application. The benefit to directors would likely be even more significant, as many directors are not well versed in statutory interpretation and application and may struggle with identifying the groups to whom they owe duties. Directors no doubt understand that they owe duties to the company, but may be confused as to their obligations towards shareholders and creditors. The imposition of a fundamental duty to the company provides a clear focus for directors, as well as a safety net of sorts through the availability of this duty as a defence. In practice the benefit would not be this universal – uncertainty will always remain as to what is in the best interests of the company at any given time, however any increased level of clarity for directors is always welcome.

B Role of creditors

Had the Law Commission's proposals been implemented in their entirety, creditors would have rather a different role within the statutory framework of directors' duties. This is because the Commission envisioned different processes through which creditors could seek to remedy breaches of directors' duties. Significantly, creditors would have no right to enforce duties while the company was solvent.[49] This differs from the way the law currently works, which allows creditors to enforce such duties.[50] Even after insolvency the Commission proposed that creditors would not be permitted to pursue an individual claim for a director's breach of duties to the company.[51] They stated that providing creditors with standing to seek remedies for breaches of solvency duties owed to the company would "undermine the statutory system for liquidations".[52] The Law Commission felt that other insolvency law provisions adequately provided protection for creditors, as well as their ability to contract for higher protection.[53]

Alongside this, the draft Act allowed for creditors to apply for an injunction where directors proposed to engage in conduct that contravenes the constitution or the Act.[54] This is a power not preserved in the 1993 Act. The implication of the removal of this proactive power from

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[49] Law Commission (R9), above n 43, at [215]
[50] Companies Act 1993, s 301
[51] Law Commission (R9), above n 43, at [215]
[52] At 219
[53] At 216
[54] Law Commission (R9), above n 32, s 126

creditors while enabling them to seek remedies for breached duties after the fact is that Parliament wanted to give creditors some enforcement ability while keeping them out of the day-to-day decision making of the company. Creditors could therefore have some influence over the company and attempt to keep it in a solvent position. In situations of insolvency, liquidators could take care of the interests of creditors.[55]

Another safeguard for creditors was the proposed s 103.[56] This would allow directors to consider creditor interests when exercising powers before insolvency. This section was only permissive and of course was subject to the fundamental duty to act in the best interests of the company. The only real effect of this section would therefore be to assure directors that they are permitted to consider the interests of creditors, so long as they recognise that they owe duties first and foremost to the company.

C Solvency

The Law Commission's report significantly included a section dedicated to a director's obligation to maintain the solvency of a company.[57] This section was later split into two, which are now sections 135 and 136 of the Act. The initial recommendation was for one section which encompassed both sustained actions and incurring individual obligations which the director believes, on reasonable grounds, will cause a risk of insolvency.[58] Section 136, which related to the incurring of obligations, is essentially identical to the second limb of the proposed s 105. The first limb however differs slightly from the resultant s 135 (reckless trading). The current section establishes the standard of reckless trading as engaging in business "in a manner likely to create a substantial risk of serious loss to the company's creditors".[59] This duty is still owed to the company, despite the direct reference to creditor interests. Section 105 of the draft Act imposed a different standard of not engaging in business "unless he or she believes at the time on reasonable grounds that the act concerned does not involve an unreasonable risk of causing the company to fail to satisfy the solvency test".[60]

These are two restatements of essentially the same duty, certainly with the same focus of protecting against insolvency. The key difference is that the proposed section provides a

[55] Law Commission (R9), above n 43, at [518]
[56] Law Commission (R9), above n 32, s 103
[57] Law Commission (R9), above n 32, s 105
[58] Law Commission (R9), above n 32, s 105
[59] Companies Act 1993, s 135
[60] Law Commission (R9), above n 32, s 105

clearer prescribed standard to be met, as opposed to the abstract wording of the current s 135. It is not as easy to objectively say what is a substantial risk of serious loss to creditors as it is to assess the risk of failing to satisfy the solvency test. This difference is minor however, as once again both are essentially protecting against the same circumstance.

D Lack of remedies

A notable omission from the Law Commission's report was a discussion of remedies for breaches of duties. The sections pertaining to derivative actions and prejudiced shareholders allowed essentially full court discretion in issuing remedies.[61] It must be assumed from this that the Commission intended remedies to be applied as they had been under the common law. Any other interpretation of this omission makes little sense.

E Summary of creditor protections

The Law Commission summarised the protections offered to creditors under their draft Act, holding these as sufficient and claiming the Act should go no further.[62] Important in drawing this conclusion was the fact that creditors are able to contract for more protection. The protections available are as follows:[63]

- The solvency test, to which all distributions are subject
- Solvency duties outlined in s 105
- Section 103, which empowers directors to consider creditor interests (subject to the fundamental duty)
- The fundamental duty to act in the best interests of the company – this protects creditors but disallowing poor management of company property
- The personal liability of directors for breaches of the solvency test and distributions of company property
- Section 126, allowing creditors to restrain proposed actions in breach of the company's constitution or the Companies Act

[61] Law Commission (R9), above n 32, ss 129 and 137
[62] Law Commission (R9), above n 43, at [216]
[63] Law Commission (R9), above n 43, at [214]

In addition, sections 104 (requiring compliance with the constitution and Act)[64] and 106 (imposing a standard of care on directors)[65] must be seen as offering additional protection to both shareholders and creditors.

IV Authorities on the application of directors' duties

A Sojourner v Robb

The issue of remedies for a breach of s 131 was addressed by the Court of Appeal in *Sojourner v Robb*. This case involved the transfer of a company's assets to a new company, in an attempt to avoid fulfilling several contracts which had been agreed to. The new company attained the staff and customer relations of the old company and continued to operate in the same way.[66] The case was brought by those unsecured creditors with outstanding contracts who were not paid upon the winding up of the initial company.[67]

The Court found that s 131 had been breached, holding that the sale price made no allowance for the goodwill of the original company. By selling the company at a price considerably under what would be "fair value" the directors did not act in the best interests of the company.[68]

The approach of the Court of Appeal in applying s 301 focussed on the equitable nature of the s 131 fiduciary duty, identifying two possible types of compensation available for such a breach of fiduciary duty. These were compensation (of a restitutionary nature) and a disgorgement of profits (or if this is not possible, a monetary award in its place).[69] Either could in theory apply here as both are based on restitutionary principles, however an order of compensation was difficult to quantify. This is because the method of calculation is to assess the difference between the sale price and the fair value price. It is far easier to say that fair value has not been paid than to accurately determine what this price is. It therefore made sense to give a monetary award in lieu of an account of profits, which the Court did.

Sojourner assists in clarifying the remedies available for breaches of s 131. However, the case is not entirely helpful when applying the principles further in other situations. This is because the facts amount to a very obvious breach of the fiduciary duty – transferring all of

[64] Law Commission (R9), above n 32, s 104
[65] Law Commission (R9), above n 32, s 106
[66] *Sojourner v Robb*, above n 3, at [61]
[67] At [10]
[68] At [46]
[69] At [60]

the company's property to another property for under value will always constitute a breached duty. The trust analogy is so obvious here that remedies are easily determined,[70] and the wider implications of this decision are difficult to distil. That being said, the case still serves as an example of how to apply equitable remedies for breaches of duties of loyalty.

B Mason v Lewis

This case involved the manager of a company defrauding two of the company's directors (the Lewises) with false invoices and generally misleading them.[71] The company eventually found itself insolvent and owing Inland Revenue $163,000 in outstanding taxes.[72] Liquidators were appointed who then initiated proceedings against the Lewises for breaching their s 135 duty to not engage in business that is likely to create a substantial risk of serious loss to the company's creditors. The Court of Appeal found that directors will be held liable for unreasonable lapses of good management practices.[73] On these facts the Court held that the company was allowed to trade for 15 months after a time when any reasonable director would have become aware of the need for close investigation.[74]

The Court outlined a test for assessing s 301 damages when a s 135 claim of reckless trading has been pleaded. This approach, which has since been applied by New Zealand Courts extensively, operates with two limbs. The first identifies the deterioration in the company's financial position between the date inadequate corporate governance became evident and the date of liquidation.[75] The second has the Court consider three factors – causation, culpability and the duration of trading.[76] These three factors were previously applied to s 320 of the Companies Act 1955, as established in *Re Bennett, Keane and White Ltd*.[77]

Causation is given little discussion here due to the clear link between the Lewises continuing to trade and this continued trading resulting in loss to the company.[78] The Court distinguishes 'culpability' from 'moral blameworthiness', focusing on the Lewises' culpability in their capacity as directors.[79] Included in this assessment is a lack of awareness of company affairs

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[70] At [144]
[71] *Mason v Lewis*, above n 74, at [114]
[72] At [27]
[73] At [83]
[74] At [75]
[75] At [109]
[76] At [110]
[77] *Re Bennett, Keane and White Ltd (in liq) (No 2)* (1998) 4 NZCLC 64,317 at [27]
[78] *Mason v Lewis*, above n 74, at [111]
[79] At [114]

and poor management. While the Lewises were unaware of the financial situation of the company, exactly this inadequate management makes them culpable of being "reckless" according to the Court's analysis.[80]

1 Is culpability an appropriate element to impose when applying s 135?

The Court of Appeal in *Löwer v Traveller* applied the fraudulent trading section of the Companies Act 1955. Adopting the same test as in *Mason v Lewis*, culpability was evaluated as a relevant factor.[81] The rationale for this came from what the Court determined to be the purposes of the section. The primary purpose of the section, per the Court of Appeal, was to "compensate those who suffered loss as a result of illegitimate trading".[82] The Court then identified a second deterrent purpose of the provision, which was used to justify the imposition of a culpability element.[83]

While s 320 was the relevant provision in *Löwer*, the court stated that Parliament's purpose was to cover the same acts of wrongdoing under the new s 135 as were addressed by the old section.[84] This resulted in the adoption of this test in *Mason*.[85] The difficulty with this position is that s 320 was concerned with fraudulent trading, which seeks to remedy a type of wrongdoing involving more blameworthiness than reckless trading does, evidenced by the intent to defraud required by the section.[86] Because of this intent requirement, s 320 could never have captured the kind of negligent misconduct resulting from a director 'sleeping on the job' which s 135 does.[87] Punishment was certainly an intended purpose of this section, and the application of a culpability requirement derived from this section to s 301 in the context of s 135 could be interpreted as implying that this section is a punitive one, rather than being strictly compensatory.[88]

While it is arguable that culpability suggests a penal nature to s 301, in the context of a s 135 claim at the very least, it could also be concluded that culpability fits within the scheme of s 135 without issue. The court in *Mason* adopted this rationalisation, framing this element as a

[80] At [83]
[81] *Löwer v Traveller* [2005] 3 NZLR 479 at [84]
[82] At [78]
[83] At [83]
[84] At [60]
[85] *Mason v Lewis*, above n 74 at [49]
[86] Companies Act 1955, s 320
[87] *Mason v Lewis*, above n 74 at [83]
[88] Peter Watts *Directors' Powers and Duties*, above n 30, at 292

necessary component to recklessness.[89] Given the statutory nature of s 135 it has not had the benefit of development through case law, and so the intended application of the section lacks the clarity of more established duties. This does seem to be a more appropriate interpretation of culpability. Accepting that it adds a penal element to s 301 would go against the clearly compensatory nature of this remedial section. Regardless of what courts have intended the culpability element to achieve when applying it, this is how such a factor should be read – as relevant in determining the type of reckless conduct envisioned when drafting s 135. Punishment should not attach to s 301 because of this element.

One way of applying culpability to s 301 without implying a punitive objective is by using this factor to mitigate compensation owed.[90] This is the best use of the element because it does not leave open the possibility of penal awards. Allowing orders to be reduced fits within the compensatory and discretionary ambit intended for s 301. To allow culpability to be used to increase relief beyond the amount of funds owed to creditors would be contrary to Parliament's intention.

2 Duration as a factor

Applying duration as a factor when determining an award under s 301 usually makes sense in the situation of a breach of s 135. This is because of the time factor inherent to this section – directors must be found to continue trading when doing so is excessively risky, and so it makes sense to ask for how long they continued to trade. Duration makes less sense, at times even no sense, when applied to some other duties. Section 136 is the most obvious example of this. The section targets a different scenario to that which s 135 seeks to remedy. Section 136 is generally concerned with the incurring of a single obligation which should not be incurred.[91] In such a situation, a duration factor is nonsensical, as each breach relates to only a single instance in time. The same can be said of many situations where s 131 applies. For example, where company property has been misapplied in a single instance, it would make no sense to assess the duration of breach. As shown below, the mixing of duties upon insolvency has resulted in this factor being misapplied.

C FXHT Fund Managers Ltd (in liq) v Oberholster [92]

[89] *Mason v Lewis*, above n 74, at [112]
[90] Peter Watts *Directors' Powers and Duties*, above n 30, at 293
[91] Companies Act s 136
[92] *FXHT Fund Managers Ltd (in liq) v Oberholster,* above n 2

This Court of Appeal case sought to reconcile when the approaches to both causation and relief, outlined in *Mason* and *Sojourner*, should respectively be applied. The court held that once the conceptual nature of the duty is identified, the test for causation logically follows this. Where the duty breached is one of loyalty or fidelity, a strict approach to liability applies and the director must show that the loss would have occurred regardless of the breach (the "but for" test). If the duty breached is one of care, more standard causation ideas apply (those which relate to the law of negligence). The onus is then on the plaintiff to show that the loss is attributable to the breach.[93]

This case provides obvious yet much needed clarification of which remedies and causation tests apply for breaches of various duties, but does little to clarify which of these are relevant in situations of multiple breaches.

D Conclusions

From these Court of Appeal cases, the "correct approach" to applying s 301 in cases of breached duties can be discerned. This is not necessarily the optimal way to enforce directors' duties, however in light of the current statute it seems to be the best result.

Importantly, this approach does not apply the elements outlined in *Mason* to every situation. Instead, remedies are matched to duties in question, based on the nature of these duties. Where multiple duties are breached it is up to the court to fit an appropriate remedy given the circumstances. This is an unsatisfactory situation to be in, as it seems that High Court judges have over-applied the *Mason* approach, as evidenced in the next part.

[93] At [28]

V How have courts applied directors' duties?

A Attractum Ltd (in liq) v Levin[94]

This case provides a typical example of how the High Court commonly assesses breaches of multiple duties. As is normal in insolvency situations, sections 131, 135, 136 and 137 were all successfully pleaded. The following is the entirety of the court's analysis when determining that these duties were breached:

> "The basis of those findings is that the Chapmans knew the Company was insolvent, they continued to trade it, they continued to divert to themselves all its revenue save immediate operating expenses, permitted the Company to default on payments of GST and permitted it to default on its ACC payments. The Chapmans did not provide financial support as they annually resolved to do, either through introducing funds or providing security. The Chapmans did not take money as employees receiving properly negotiated salaries. They took the Company's money in their capacities as controllers and owners."[95]

The succinct nature of this analysis is not necessarily problematic as the breaches were very clear. More concerning is the lumping of all of these duties together. This demonstrates the lack of inherent distinction between these duties, which has been furthered by the lazy application of duties by the courts. For the most part courts will get away with this general analysis without causing injustice. This is because generally the conduct of directors is relevant to multiple breached duties. However, in situations where misconduct is varied, courts may fail to match duties to the individual mischiefs they seek to remedy. This results in great uncertainty as to the conduct towards which each duty is directed, and leads to a more uncertain enforcement regime of duties.

If this trend continues it seems likely that remedies will be misapplied in certain situations. For example, if all duties are dealt with together, courts may require culpability (a relevant factor for s 135) to be high before an order is made. Should this threshold be unmet, relief may be withheld. This would be inappropriate in a situation where both ss 131 and 135 have been breached, as s 131 need not invite this requirement to be met. Such a broad approach in

[94] *Attractum Ltd (in liq) v Levin* [2020] NZHC 318
[95] At [19]

situations of multiple breach is extremely common. This case exemplifies a trend which can be found in nearly every insolvency case where directors are being pursued for breached duties by creditors.

B Grant v Independent Livestock 2010 Ltd [96]

This case demonstrates the muddling of duties and subsequent over-application of the *Mason* approach when applying s 301. The facts involved the director of a company taking extreme steps to avoid transferring funds to Mr and Mrs Mudge, whose stock had been sold by the company on their behalf. The director's misconduct included claiming a commission for the sales, something which had not been agreed to.[97] The company eventually reached a point of liquidation, and the money outstanding characterised Mr and Mrs Mudge as creditors.[98]

Potter J found a clear breach of s 131.[99] Moving to s 135, the Judge concluded that while the director caused the business to be carried on in a manner likely to cause loss to creditors, this did not fit the requirements of s 135.[100] This conclusion involved an odd interpretation of s 135, as the Judge conceded that the test outlined in the section had been satisfied.[101] The rationale for concluding that s 135 was not breached was that no "risk" was incurred with the objective being commercial advantage.[102] This was further justified by the fact that the director's "evasive behaviour" occurred, for the most part, when the company was financially sound.[103] Overall, the Judge found no breach of s 135, relying heavily on what they perceived to be the purpose of this section.

The Judge correctly identified that s 131 more appropriately applies to these facts, however it is odd that s 135 was so readily abandoned. Furthermore, the other alleged breaches were not considered due to the clear nature of this s 131 breach. Regardless of the merits of this reasoning, it is the subsequent application of s 301 which is the primary cause for concern. This is because Potter J applied the *Mason* elements of causation, culpability and duration when applying s 301.[104]

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[96] *Grant v Independent Livestock 2010 Ltd* [2012] NZHC 3458
[97] At [158]
[98] At [109]
[99] At [159]
[100] At [169]
[101] At [166]
[102] At [167]
[103] At [168]
[104] At [176]

The imposition of these elements establishes an unnecessary hurdle for the creditors to overcome before receiving relief. In most insolvency situations where s 131 is breached, s 135 is also breached. This makes applying these factors forgivable, as often the s 135 breach is the most obvious and relevant breach. This is not such a situation, as the misconduct of the director clearly demonstrates behaviour in bad faith. The appropriate remedy here would have been to order compensation of a restitutionary nature for the loss incurred as creditors of a company now in liquidation, or alternatively an account of profits. Causation flowing from such a breach should be strict, requiring no consideration of culpability.[105]

It is likely that the result of this case would have been no different had the correct approach been taken to applying s 131. This is because relief was granted, and the discretionary nature of s 301 allowed the court to prescribe the correct quantum of this relief. However, had the creditors failed to sufficiently establish the elements of causation, culpability and duration, relief would not have followed. This would be unjust because these elements need not be established. Furthermore, such an outcome is entirely conceivable, given the frequency with which these factors are applied. This demonstrates the problems arising from the general lack of clarity which still persists in the framework of directors' statutory duties.

C Hansa Ltd (in liq) v Hibbs [106]

Hansa v Hibbs is a recent High Court case which primarily addressed s 136. While many other duties (ss 131, 133, 135 and 137) were also successfully pleaded [107], both the plaintiff and the Judge focussed s 136 when applying s 301, due to an emphasis on this section in the plaintiff's pleadings.[108] The conduct to which a breach of s 136 is attributed involved the incurring of many debts which the company could not repay.[109] Because of the continued nature of these breaches of the section, the court sought to determine the duration over which these breaches occurred when applying s 301.[110] They then identified a causative link between the director's actions and the subsequent losses incurred, before determining that this director's culpability was high.[111]

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[105] *Sojourner v Robb,* above no 3
[106] *Hansa Ltd (in liq) v Hibbs* [2018] NZHC 2014
[107] At [47] [53] [55]
[108] At [31][56]
[109] At [38]
[110] At [58]
[111] At [59]

The court was not technically wrong in applying this test from *Mason*, as s 135 (among other duties) was breached. However, by not specifying that remedies were intended to be centred around this reckless trading provision, and by emphasising the application of s 136 over other duties both expressly and through the far more detailed analysis of this section's breach, the implication of the court's decision is that this interpretation of how s 301 is to be applied related directly to s 136.

This cannot be the correct way to apply s 301 in situations where s 136 has been breached. The primary reason for this is that s 136 is intended to apply to individual obligations incurred when they should not have been. Duration should not be applied in such situations, as the duty is intended to target a single instance in time, rather than a series of breaches. This conclusion is bolstered by the existence and intended purpose of s 135. Where s 136 targets a singular instance of breach, s 135 is intended to apply where a director commits a continued breach by putting the company at risk of insolvency.

Even if many breaches of s 136 have occurred over time, relief should focus on the value of each individual obligation incurred, rather than the company's deterioration generally. While s 136 was emphasised here, s 135 would have been better suited. The continued manner of the risky trading is exactly what s 135 is intended to remedy.

This misidentification of what sections 135 and 136 are respectively trying to achieve started with the emphasis on this duty by counsel.[112] The court then failed to identify that s 136 was being slightly mispleaded, and continued with such an interpretation of the section. It seems that the problem of misapplying duties (relative to how they were intended to be applied) has generally been a result of poor pleading by counsel, specifically the muddling of duties through over pleading. This is not necessarily the fault of lawyers. They have prudently identified that they can plead every duty (or near to it) under the Act, and in all likelihood, one will result in a successful claim.

D The Hedley approach to remedies and causation

The High Court in *Hedley* demonstrated an appropriate application of multiple duties. The court outlined the remedies which would be ordered should breaches of sections 131 and 137 be found. They then noted that double recovery is not available.[113] Importantly, the court stated: "as the two sections are based on different rationales, s 131 being fiduciary in nature

[112] *Hansa Ltd (in liq) v Hibbs*, above n 126, at 31
[113] *Hedley v Albany Power Centre*, above n 12, at [27]

and s 137 being based on negligence principles, it is advisable to separate them out."[114] The court then referenced *Bank of New Zealand v New Zealand Guardian Trust Co Ltd*, an instrumental case in determining issues of remedies and causation.[115] This case identified three types of breaches of duty by trustees and other fiduciaries, which are applicable in a company law setting:

a) Breaches leading directly to damage to or loss of the trust property;
b) Breaches involving an element of infidelity or disloyalty which engaged the conscience of the fiduciary; and
c) Breaches involving a lack of appropriate skill or care [116]

As observed by the High Court, breaches of s 131 fall into the first and/or second categories, whereas breaches of s 137 fall into the third.[117] These categories determine the appropriate causation test to be applied in each situation. When seeking an account of profits, one need only point at the profits attained and establish a breach. The party in breach must then establish that the profits would have been obtained regardless of the breach.[118] Where equitable compensation is the desired remedy, a Court must ask: "but for" the breach, would the loss have occurred?. Section 137 differs, adhering to standard principles of causation and remoteness in the law of torts.[119]

The significance of matching remedies and therefore causation tests with the appropriate breached duty is not often relevant. This is because, in cases of insolvency, many duties have usually breached, and relief will be ordered regardless of the method applied. However, situations can be imagined where only one duty has been breached and liability turns on a determination of causation. In such a scenario courts may require that an unnecessary causation requirement be met, imposing a greater standard than Parliament intended. This is the problem created by the lack of distinction between duties.

E Cooper v Debut Homes[120]

The Supreme Court very recently clarified how the law surrounding directors' duties should be applied in situations of multiple breaches. The court confirmed that, in circumstances

[114] At [27]
[115] *Bank of New Zealand v New Zealand Guardian Trust Co Ltd* [1999] 1 NZLR 664
[116] At p 687
[117] *Hedley v Albany Power Centre*, above n 12, at [30]
[118] *Hedley v Albany Power Centre*, above n 12, at [33]
[119] *Hedley v Albany Power Centre*, above n 12, at [37]
[120] *Cooper v Debut Homes (in liq)* [2020] NZSC 100

where several breaches have occurred, "any redress under s 301 must be tailored towards the combination of breaches found." [121] They recognised that breaches of s 135 will generally lead to an assessment of the deterioration in the company's financial position between the time when trading should have ceased and the date of liquidation.[122] By contrast, s 131 may encompass a far wider range of breaches, depending on the nature of the breach.[123] Relief will therefore vary more for such breaches. For example, situations of misappropriated funds may lead to a tracing action. By contrast, the incorrect use of information attained in the course of being a director might warrant an account of profits, possibly even leaving room for an allowance to be made for the skill and effort of the director.[124]

Perhaps the greatest clarification offered by the Supreme Court relates to s 136. The court prudently identified that s 136 is distinct from s 135, as it concentrates not on the general financial deterioration of the company, but on individual obligations incurred.[125] The best way to remedy this harm is to reverse it, and this is achieved through restitutionary relief.[126] Important in reaching this conclusion was the observation that, if compensation is limited to net deficiency as it generally is for s 135, directors might be incentivised to continue trading while keeping this deficiency constant.[127]

The essence of the Supreme Court's instruction on how to apply s 301 is that "the appropriate relief must respond to the duty or duties actually breached."[128] This confirms the idea that remedies should be matched to duties breached, however does not confine restitutionary relief to fiduciary duties and damages to duties of care. The court allows more discretion, stating that restitutionary relief can be available for duties which are not fiduciary in nature.[129] This statement essentially licences courts to match remedies to situations of breach as they see fit. This allows for more creativity and discretion when issuing remedies than permitted by previous authorities, such as *FXHT*, but also strays further from any clear, formulaic approach to making such orders.

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[121] At [162]
[122] At [164]
[123] At [163]
[124] *Chirnside v Fay* [2004] 3 NZLR 637
[125] COOPER, at [165]
[126] At [165]
[127] At [166]
[128] At [160]
[129] IBID

This decision shows that the Supreme Court has failed to identify the mess of duties manifesting in the High Court. Adding more discretion may work where the court takes care to distinguish between duties, however this is not the case at the lower judicial level. Nothing in the judgment provides a clear statement that courts should confine the *Mason* approach to s 135 cases. The court even states that culpability will be relevant for any decision of quantum – be it compensatory or restitutionary.[130] This is not incorrect for the vast majority of cases – s 135 is pleaded so often that culpability will usually be relevant. However, in a situation such as that of *Sojourner* and other equitable breaches, culpability would be inappropriate to consider. The appropriate relief in such a case is to reverse the wrong by ordering an account of profits – culpability has no place in such a decision. Similarly, situations of misappropriated funds may lead to an action in tracing. Culpability again is irrelevant here, and to apply it would provide a hurdle for creditors to surmount which should not be required, resulting in an interference with the proprietary nature of the remedy.

The same applies where s 137 is breached. If s 137 is truly a restatement of the common law duty of care, culpability should not be considered. If s 137 were intended to be something other than this common law duty, at least where relief is relevant, Parliament would have indicated this in the statute.

1 Conclusions on Cooper

The conclusion of this case is therefore that it may help higher courts to reconcile situations where multiple duties are breached, but is unlikely to amount to any change in the High Court. A clear condemnation of the overuse of the *Mason* approach may be the only thing to achieve this, short of Parliamentary action.

Situations where s 136 are applied may be the exception. The court does a good job of clarifying what this duty seeks to achieve and how it should therefore be applied. In the future, the High Court may do a better job of identifying situations where this duty is relevant and matching restitutionary remedies to breaches. This section has been overshadowed by s 135 in the past and has subsequently experienced a dearth of individual analysis in the Court of Appeal and Supreme Court.

F Conclusions on High Court cases

130 *Cooper* at [162]

Due to the recency of the Supreme Court's judgment in *Cooper*, none of the High Court judgments discussed have had the benefit of relying on this decision. It is unlikely that the results in these cases, or any of the numerous other High Court cases of a similar nature, would differ in light of this decision. Perhaps *Hansa* would now be applied differently, as the court might identify that while many breaches of s 136 have occurred, s 135 is better equipped to deal with these breaches collectively.

VI UK Law

A Overview

The law of directors' duties in the UK has a similar form to that in New Zealand, however is spread across two statutes. The Companies Act 2006 lists general duties owed by directors. For the most part these duties are very similar to our own, with minor changes to wording, for example directors must promote the success of the company, rather than acting in its best interests.[131] The primary differences between the UK law and our own comes in remedying situations of insolvent/reckless trading. Section 174 outlines a duty of care essentially identical to our s 137.[132]

Section 178 of the Act states that the consequences for a breach of a general duty are the same as would apply if the breach occurred at common law or in equity.[133] While our Companies Act contains no such provision, New Zealand Courts have interpreted the Act in the same way as this.[134] The section further clarifies that all of these duties are fiduciary in nature, other than the s 174 duty of care. This greatly assists UK Courts when it comes to issuing remedies, as they need only look to equitable remedies and causation tests (or lack of) when applying duties. Similarly, where a breach of s 174 is alleged, Courts can apply well-founded common law principles which have developed with the law of negligence. As established, New Zealand Courts have struggled when applying duties due to a lack of clarification surrounding the nature of some of these duties (namely sections 135 and 136).

The UK statute contains no equivalent of New Zealand's s 301. Because of this, and the fact that duties are owed to the company and not directly to creditors, creditors cannot bring claims for breached duties in times of solvency. In cases of insolvency or near insolvency it has been held that directors must consider the interests of creditors.[135] Despite this, the duty is still owed to the company **[PHD 197]**.[136] Creditors therefore must rely on the company to enforce this, and cannot bring independent claims **[PHD]**.[137]

The equivalent of our reckless trading provision can be found in the Insolvency Act 1986. This Act includes a wrongful trading provision (s 214)[138] and a fraudulent trading section (s 213).[139] Just as our reckless trading provision contains no mention of "recklessness", the UK

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[131] Companies Act 2006, s 172
[132] Section 174
[133] Section 178
[134] **FXHT ABOVE**
[135] **NICHOLSON ABOVE**
[136] Hariati Mansor "Solvency, Company Directors' Duties and the Problem of Process and Enforcement – A Comparative Study" (LLB (PhD) Dissertation, University of Waikato, 2011) at 197
[137] Ibid
[138] Insolvency Act 1986 s 214
[139] Section 213

section does not mention “wrongfulness”. The section is satisfied where a company has reached insolvency, and at some time before this occurred a director “knew or ought to have concluded that there was no reasonable prospect that the company would avoid going into insolvent liquidation”.[140]

Section 214(4) states that courts must consider both an objective standard for the skill and experience that may reasonably be expected of a director in that position, as well as the subjective knowledge, skill and experience of the director in question. This section is only enforceable on the application of liquidators – creditors may not bring a claim for a breach of ss 213 or 214.[141]

B Consequences of the UK approach to wrongful trading

By virtue of not allowing creditors to bring claims for breached duties, the UK has not experienced the same degree of confusion in application as New Zealand has. This is because duties owed generally have not become muddled with insolvency-targeted duties, as these duties reside in different statutes and apply in slightly different circumstances. The trade-off for this added clarity is less protection for creditors, as they are not able to bring claims at all and must rely on the proactiveness of liquidators.

Both of these features of the UK law have allowed the duties owed by directors generally to develop independently of those owed in times of insolvency. While the UK law no doubt has issues, it has at the very least not allowed duties intended to be applied in insolvency to disrupt the clarity of the scheme of directors’ duties as a whole.

VII Critique

A Conclusions from the High Court case law

1 Section 301

[140] Section 214
[141] Above, n 143, at 254

A clear trend which has arisen through much case law is that s 301 has caused much confusion. This is added to by the inherent overlap between duties, a result of a poorly constructed Act which fails to distinguish duties sufficiently, as well as the muddling of duties and their means of application which has come with over pleading.

One of the biggest issues with s 301 is its failure to clarify the approach to be taken, in terms of causation and remedies, when multiple duties are breached. This is particularly problematic when considering the overlap between duties, as nearly every application of s 301 involves multiple breaches of duties. This was an entirely foreseeable consequence of the codification of duties because of the similarities between such duties. For example, ss 135 and 136 both deal with insolvency, and are both products of the same section proposed by the Law Commission. Other jurisdictions, such as the UK, have mitigated the extent of this confusion by separating solvency duties from those owed generally by directors. Parliament must have envisioned much overlap between these duties and others when they allowed creditors to make claims for any breach in times of insolvency, and yet no assistance is offered for such situations.

2 The High Court application of Mason/Sojourner

It seems that the High Court has struggled to find a consistent and appropriate method of applying s 301 for breaches of directors' duties. This is exemplified through the constant desire to fit the *Mason* elements to any set of facts. Perhaps the pleading of nearly every duty in times of insolvency has resulted in this overuse of this approach, as s 135 (the relevant duty for this applying this method) is very rarely left off the list of alleged breached duties. This has given an unrealistic picture of cases where such an approach is appropriate.

There seem to be several reasons which have resulted in this confusion: lawyers have become accustomed to pleading breaches of every duty in times of insolvency, the statute is constructed poorly and does not distinguish duties well in relation to the conduct they seek to remedy, and Courts have also not done a good job at emphasising these distinctions. Regardless of the reasons for this, the factors of causation, culpability and duration have become staples of High Court Judges in cases of insolvency.

This is problematic because it allows Courts to lose sight of the need to match remedies and duties to the mischief at hand. Culpability is regularly assessed, yet culpability is not a relevant factor where the breach is of a fiduciary duty or a director has acted negligently. Similarly, duration will not generally be relevant for breaches of ss 131 and 136.

Once again, this is generally not problematic because in cases of insolvency s 135 will almost always be relevant. As only a limited sum can be awarded to creditors, the method of determining an award under s 301 is not usually important. The Court can apply the *Mason* approach and find the full amount of compensation through this avenue, ignoring the other successfully claimed breaches of duties when it comes to applying s 301 other than to add to the culpability under a 135 assessment of damages. The question then arises: if s 135 is always or nearly always pleaded, is it problematic to apply this approach?

B Conclusion

The law as it currently stands is unsatisfactory and has not resolved the issues of inaccessibility and a lack of clarity identified by the Law Commission almost 30 years ago. The fundamental reason for this is the drafting of the statute. There are too many duties in the Act which cover similar situations, and this has resulted in uncertainty as to what type of mischief each seeks to remedy. This problem has been added to by the inclusion of duties which are intended to avoid situations of insolvency with other, more general, duties. Had these duties been separated from the others, as is the case in the UK and as was proposed by the Law Commission, it would be far less likely that courts would confuse duties as frequently as they do.

The most problematic result of the over pleading and subsequent mixing of duties comes from s 135. The factors of culpability and duration have bled into the analysis of other duties, and at times through enforcement these other duties have been made to overcome more onerous requirements than should be the case. The shared enforcement provision of s 301 coupled with the uncertainty surrounding this section's application, particularly in situations of multiple breaches, does nothing to alleviate this confusion.

I believe that several of the Law Commission's proposals would have lessened the problems the statute currently experiences, although may not have resolved them. The solvency section proposed was preferable to sections 135 and 136. This is because of the increased clarity as to the standard to be met, as well as the clear wording indicating that the duty is intended to be a duty of care (through use of a "reasonableness" test). Section 135 loses much of its clarity by referencing "recklessness" only in the title – leading to much uncertainty as to its purpose.

Furthermore, a hierarchy of duties as suggested by the Commission would have provided more certainty for courts when applying multiple duties, a scenario which has proven to be very common. As double recovery is not permitted under s 301, courts often have to choose

which duty to apply to this section to issue remedies. Clarifying that s 131 is the fundamental duty would have resolved this easily. Despite this, confusion may have remained in situations where s 131 does not apply.

Adopting an approach similar to the UK might also assist in adding clarity. Separating out solvency targeted sections – ss 135 and 136 – from the application of the other duties would remove the potential for applying each duty to become confused.

While the statute leaves much to be desired, it has not been assisted by the way in which the High Court applies these sections. Several cases in higher courts have resulted in statements that the principles relating to s 135 should not be applied to other sections. These cases have also stated how to approach potential s 131 breaches. The problem is that little help has been offered as to how remedies should be determined where multiple breaches occur. *FXHT* stated that remedies should be matched to the nature of the duty breached, but provided no assistance in cases of multiple duties. *Cooper* provided a contrary solution – that remedies can be matched to any duty regardless of the nature of each, so long as the matching is appropriate. This discretion will be unlikely to assist the High Court in its future endeavours in company law.

A conclusion of this dissertation is that the over pleading of duties, particularly s 135, in insolvency cases has revealed an unrealistic picture of how s 301 is to be applied. The obvious counter argument to this is that this unrealistic picture is self-created: by only reviewing creditor's claims, of course insolvency situations will be over-represented. Creditors will generally only make claims in situations of insolvency, as in such cases they have lost money. While this is true, it hardly matters.

The fact that creditors are enabled by the Act to make claims while the company remains solvent is enough to warrant concern. It is conceivable that a creditor could make a claim in relation to a solvent company for breaches other than s 135. In such circumstances, there is no reason to assume that a court would order the correct remedies or apply the appropriate causation test. The evidence from the application of duties in insolvency cases would suggest the opposite.

In conclusion, nearly 30 years after the introduction of a statute intended to make the law more accessible, clear and easy to enforce, it remains clear that these objectives have not been achieved. No doubt the law is in a more certain spot than it was before the Companies

Act 1993, due partly to the codification of duties, however reform would have the potential to provide much needed clarity to the law of directors' duties.

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