

Are large companies really paying legal dividends?

Published: January 14, 2026, 3:00 pm

What this post is about

This post deals with a technical issue that is, however, of enormous significance to the UK and other economies.

There is accumulating evidence that the largest companies in the world are overpaying dividends to keep their shareholders happy, and are using debt to do so. They are significantly increasing the risk in the economy as a result. They are also denuding themselves of the funds needed to tackle climate change as a result. As a consequence Adam Leaver at Sheffield University Management School and I have been looking at the legality of these payments, and what may be done to ensure that companies comply with both the spirit and the letter of the law at this critical time. The corporate sector's success in tackling climate change may depend upon them doing so. As we have shown, the legality of their actions is in doubt, as is their accounting. Reform is overdue.

Hollowed out firms

Last year I co-authored with Prof Adam Leaver at Sheffield University Management School and others a paper that looked at the phenomena that we describe as '[hollowed out firms](#)'. These are companies where it would seem that financial engineering has a higher priority than actually generating profits for payment to shareholders.

One of the characteristics of these groups of companies that we have identified is an apparent ability to pay dividends in excess of the level of profits reported in the accounts of the group as a whole. This is possible because the capacity to pay dividends is not based on the group accounts, but is instead based upon the accounts of the group parent company, considered in isolation. This means that the profit available for distribution depends upon the ability of group subsidiary companies to distribute realised profits that they have made, calculated in isolation, to that group parent company without having to take into account the losses of other group subsidiaries that might otherwise dilute those distributable profits. The result is that

there are many entities where the group as a whole looks to have negative revenue reserves, but the group parent company considered in isolation appears to have many reserves available, from which dividends can be paid.

This is, as far as we are concerned, an issue of considerable significance. That is partly because of the scale of this apparent persistent overpayment. [As we have noted](#):

The findings show that in the latest available accounting year, a significant minority of firms are paying out more to shareholders than they generate in net income. 37 per cent of S&P500 firms distributed more via dividends and share buybacks than they generated in group net income. The figures for the FTSE 100 and S&P Europe 350 were 28 per cent and 29 per cent respectively. A sizable number of firms borrow heavily in order to do this.

The obvious question to ask is why this might be legal. Adam Leaver and I have continued to work on this issue, and have had meetings with the relevant government department - the Department for Business, Energy & Industrial Strategy - about it. As a result, we have now published two papers that we have submitted to them this week.

Why capital maintenance matters

The [first, shorter, note](#) refers to our reasoning on why we think this issue of capital maintenance in companies is so important. We felt it necessary to reiterate this as we feel that its significance is understated in the BEIS consultation on auditing, and we note our reasons for doing so. We do, in particular, argue that

- * Recent corporate collapses show that when strategically important companies fail, they impose a social cost that may involve government support.*
- * All stakeholders, including shareholders, creditors, the workforce, tax authorities, regulators and government, therefore have an interest in ensuring that companies are resilient and can stand on their own two feet under adverse conditions.*
- * This idea is enshrined in the principle of capital maintenance. This is set out in the 2006 Companies Act which requires that the protection of capital should be the superordinate legal duty of directors.*
- * Our view is that this principle has been eroded as directors have pursued a more aggressive approach to profit realisation and shareholder distributions which has hollowed out firm redundancies. We also believe that auditors and regulators have failed to act with sufficient robustness on this issue.*
- * Our view is that this practice is becoming systemic because it is rooted in the overly-permissive guidance provided by professional accounting institutes on distributable profits (i.e. ICAEW 2017).*

I have added the emphasis.

I also highlight the last point. This guidance from the ICAEW is most especially worrying as it is treated as having the status of law when there is no way that this can be the case, and it is this guidance that, above all else, that permits that dividends might be paid when the available distributable reserves to do so are not available within a group - which we think dangerous to that group's creditors and to its long term ability to survive, which we think of importance.

How to get the law on dividends payable right

This [then led us to the second, longer, note](#). This refers to why we think the existing framework for distributing retained reserves is not actually legal. In summary, distributions of dividends must be made with reference to a company's accounts, and as we note in our document the law requires that those accounts must include a profit and loss account. However, since the individual entity or separate accounts of a parent company of a group do not have to, by law, include a profit and loss account these cannot form the relevant basis for estimation of distributable reserves as a consequence. This appears to be a simple statutory fact. As such the ICAEW guidance from 2017 that claims that these individual entity or separate accounts of a parent company of a group can be used for this purpose must, in our opinion, be recommending an illegal practice. In our opinion it does necessarily follow that a new basis for estimation of these reserves is required.

In the first instance, we suggest that this estimate must necessarily be based on group reserves for the reasons noted above. Second, we argue that the figure from the face of the accounts is also not fit for this purpose because that figure can include what are called unrealised reserves. These are profits that have been recorded for accounting purposes but which have, in effect, no cash consequence e.g. because they might arise from revaluations. In that case, that figure for reserves has to be split in two i.e. between those that are realised, and so capable of distribution, and those that are not capable of distribution because they are unrealised.

In the paper, we set out three bases for the estimation of this split, of which the last is by far the best. The argument that we have heard used is that this split cannot be made because the records to identify it do not exist, or the complexity of groups now prevents it on an ongoing basis. As a result it is argued that existing arrangements should continue. Because we believe that those existing arrangements might impose a considerable cost on society we disagree, which is why we have shown that we think estimation is an entirely possible thing to do.

Why this matters

This issue matters in our opinion for four reasons.

Firstly, we think that there are far too many companies now trading in the UK that are vulnerable to corporate failure because they have taken on excessive debts to pay

dividends that their group accounts cannot support on the basis laid out in what we think UK law says. Quite simply, if a group has negative reserves then whatever the accounts of the parent company considered in isolation might show it is our belief that the overall true and fair view of their activities suggests that the payment of any dividend might be imprudent and prejudicial to the interests of its creditors, whether they arise from trading, or are its employees, or its tax authority. Such is the size of many of these companies that the disruption that might result from their failure is far too significant for this issue to be ignored.

Second, we happen to think that the compliance by companies with both the spirit and letter of the law is necessary if business is to be undertaken on a level playing field, and there are some signs at present that this is not the case, with some companies appearing to comply with the requirements that law seems to indicate appropriate in this area and with others making dividend distributions that we think are of questionable validity. There is clear indication that this is disrupting the allocation of capital within financial markets in favour of those who are over distributing, and that this might be increasing risk for shareholders, pension funds and others who are dependent upon such investments in a way that we consider unacceptable.

Third, at a time of economic uncertainty we think that the issue that we are addressing is of increasing significance.

Fourth, that sentiment is only exacerbated by our heightened awareness of the significance of climate change. It is now apparent that many UK companies are going to be subject to considerable financial pressure as a consequence of their need to transform their businesses if they are to become net-zero compliant. The retention of appropriate reserves within their accounts for this purpose is becoming increasingly important. Sustainable cost accounting might indicate the necessary level of those reserves, which would be considered realised reserves for the purposes of dividend calculation, meaning that they would reduce the capacity of a group to pay dividends until net-zero compliance was achieved. As a consequence, we think that a change in the basis of the recognition of the nature and quantum of reserves for the purposes of dividend calculation is a fundamental part of preparing accounting for the climate crisis issues that it has to face.