



Business Law Briefing No: 1

Director's Duties – Private Companies

The Companies Act 2006 (the "Act") lays out the seven general duties of Directors which reflect and codifies the law before the Act. In addition, however, the Act also makes it easier for shareholders to bring an action in the Company's name. This power of the shareholders in addition to both the Courts and the various regulatory bodies open stance to make directors more accountable for their actions means that every person holding office ignores their responsibilities at their peril and may expose themselves to personal liability,

The seven general duties are laid out in the Act and are as follows:

A duty to act within the powers of the Company

This means to act in accordance with the powers set out in the Company's Articles of Association and only for the purposes for which those powers were conferred.

A duty to promote the success of the Company

A director must act in a way he or she considers, in good faith, would be the most likely to promote the success of the Company for the benefit of the members as a whole. This duty used to be referred to as "acting in the best interests of the Company", however, the Act goes on to add a list of further requirements so broadening the scope of this duty. The Director, in considering such action must have regard amongst other things to:

- The likely consequences of any decision in the long term;
- The interests of the Company's employees;
- The need to foster the Company's business relationships with its suppliers, customers and others;
- The impact on the Company's operations on the community and the environment;
- The desirability of the Company maintaining a reputation for high standards of business conduct;
- The need to act fairly as between the members of the Company; and
- If the Company is in solvent, the interests of the Company's creditors.

A duty to exercise independent judgment

The Director must exercise independent judgment but this duty is not infringed by he or she acting;

- In accordance with an agreement entered into by the Company that restricts the future exercise of discretion by its Directors; and
- In a way authorised by the Company's constitution.

A duty to exercise reasonable care, skill and diligence

This means the care, skill and diligence that would be exercised by a reasonably diligent person with:

- The general knowledge, skill and diligence that may reasonably be expected of a person carrying out those functions carried out by the Director in relation to the Company; and
- The general knowledge, skill and experience that the Director has.

This is, therefore, an objective and a subjective test. For example, a higher duty would be expected of an experienced director of an established company compared to an inexperienced director who has just started out. Similarly, solicitors or accountants who are also directors would be deemed to have a higher level of general knowledge and skill by virtue of their qualifications and training.

A duty not to accept benefit from third parties

A director must not accept any benefit from a third party conferred by reason of he or she being a director or by he or she doing (or not doing) anything as a director. However, this duty is not infringed if the acceptance of the benefit cannot reasonably be regarded as a conflict of interest or duties.

A duty to avoid conflicts of interest

Conflicts of Interest have always existed and occur in many situations such as where a director is:

- A shareholder of the Company
- A customer or supplier of the Company
- A director of another company who has dealings with or is in competition with the Company
- An advisor (e.g. financial, property agent or legal) to the Company
- A Trustee of the Company's Pension Fund

This list is not exhaustive but is intended to give an indication of the types of transaction that may possibly give rise to a conflict. Under the old regime, if a conflict arose then the director concerned had to take steps to reduce the effect of the conflict by not taking part in any board discussions or voting on any board resolution relating to it. However, the Act has created an **absolute requirement** for directors of private companies to avoid a situation in which he or she **has, or potentially could have a direct or indirect** interest that conflicts, or possibly may conflict, with the interests of the Company.

The Act further stipulates that this duty applies in particular to the exploitation of any property, information or opportunity and **it is immaterial whether the Company could take advantage of the property, information or opportunity.**

However, the Act does provide that this duty will not be infringed if:

- the matter has been authorised by the non-conflicted directors of the Company and the meeting was quorate without the conflicted director(s); and
- the Company's constitution does not invalidate the directors' authorisation.

If the conflict of interest arose before 1st October 2008 then the law that applied at the date the conflict applied. Conflicts arising on or after 1st October 2008 are subject to then new law with the added requirement in respect of private companies formed before 1st October 2008 where in all cases the members need to resolve to give the directors the power to authorise the conflict of interest.

Duty to declare the interest in the proposed transaction or arrangement

The declaration by the director of a conflict of interest in a proposed transaction must be given in before the proposed transaction takes place and if such declaration proves to be, or becomes inaccurate or incomplete, then a further declaration must be made.

The declaration can be made either at a meeting of the directors or by notice in writing to the other directors. It is possible for a director to give a general notice that he or she has an interest in another body corporate or firm (and or is connected with a specified person) and is regarded as being interested in any transaction or arrangement that may, after the date of the notice be made with that body or firm (or person).

What should happen next?

It is essential that all companies carry out a review of their directors' interests and establish whether there are any potential conflicts with the interests of the

Company. For private companies formed before 1st October 2008 the Articles of Association must be reviewed and the appropriate amendments made. For advice on this and all other corporate matters do not hesitate to contact us.

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