

DIRECTORS' DUTIES

The Guernsey Society of Chartered and Certified Accountants

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Introduction

- Types of director
- What are directors' duties?
- Consequences
- The Code

Types of director

- Various types of director:
- *De jure* director
 - “legal director”
 - Appointed pursuant to the Articles (by board or by members)
- Alternate Director
 - Appointed to act on behalf of a director
 - Articles govern the appointment, entitlements, powers and termination
 - Considered a director for purposes of the Law
 - Must notify Registrar of appointment

Types of director

Some who do not 'exist'! (perhaps)

- Nominee Director
 - No such concept of nominee directors appointed simply as a “watchdog”
- Non-Executive Director
 - A director who is not an employee of the company - considered independent
 - No distinction between executive and non-executive in the Law, but maybe in the law?

Re Barings plc and others

- (i) Directors have, both collectively and individually, a continuing duty to acquire and maintain a sufficient knowledge and understanding of the company's business to enable them properly to discharge their duties as directors.*
- (ii) Whilst directors are entitled (subject to the articles of association of the company) to delegate particular functions to those below them in the management chain, and to trust their competence and integrity to a reasonable extent, the exercise of the power of delegation does not absolve a director from the duty to supervise the discharge of the delegated functions.*
- (iii) No rule of universal application can be formulated as to the duty referred to in (ii) above. The extent of the duty, and the question whether it has been discharged, must depend on the facts of each particular case, including the director's role in the management of the company.*

Types of director

Equitable Life Assurance Society v Bowley and others

*It is well known that the role of non-executive directors in corporate governance has been the subject of some debate in recent years. For present purposes ... it in any event suffices to say that the extent to which a non-executive director may reasonably rely on the executive directors and other professionals to perform their duties is one in which the law can fairly be said to be developing and is plainly 'fact sensitive'. **It is plainly arguable, I think, that a company may reasonably at least look to non-executive directors for independence of judgment and supervision of the executive management.***

Types of director

Some who might not realise it!

- Shadow Director
 - *De jure* Directors of the company accustomed to act in accordance with their directions or instructions
 - Not applicable where acting on advice given in a professional capacity, but ...

Buzzle Operations Pty Ltd (In Liquidation) v Apple Computer Australia Pty Ltd

- Habitual compliance over a period of time is required
- Requires a causal connection between third parties wishes and director's conduct

Types of director

- *De facto* director
 - Individual carrying out the functions of a director
 - Manner of appointment irrelevant
 - Undertakes functions only properly discharged by a director of the company

What are directors' duties?

- Duties owed by a director to the company
- English duties are expressly codified under Companies Act 2006
 - Include acting within powers; promoting success of the company; exercising independent judgment; exercising reasonable care, skill and diligence; avoiding conflicts of interest; not accepting benefits from third parties; declaring interests in proposed transactions/arrangements
- In Guernsey there are however no expressly declared duties under the Law (but they are certainly in there!)
- Directors are fiduciaries: owe fiduciary duties to the company
 - Based on common law concepts
 - Similar to duties owed by trustees
 - Solvent and Insolvent duties

‘Solvent’ duties

- Management
 - Business and affairs of the company to be managed by (or under the supervision of) the directors
- Honesty
 - Must act honestly and for a proper purpose
 - Best interests of the company as a whole
- Conflicts and profits
 - Only profit from position of director in accordance with Articles and/or member approval
 - Avoid any conflict between duty as director and any other duties/interests (unless authorised by Articles)
 - Provisions in the Law for declaring interest in transactions

Solvent duties

- Duty of care and skill
 - Exercise such skill and care as expected from someone of the same level of skill, knowledge and experience

Care and Skill



Insolvent Duties

How are they any different?

- Creditors and Members respective interests

'In a solvent company the proprietary interests of the shareholders entitle them as a general body to be regarded as the company when questions of the duty of directors arise. If, as a general body, they authorise or ratify a particular action of the directors, there can be no challenge to the validity of what the directors have done. But where a company is insolvent the interests of the creditors intrude. They become prospectively entitled, through the mechanism of liquidation, to displace the power of the shareholders and directors to deal with the company's assets. It is in a practical sense their assets and not the shareholders' assets that, through the medium of the company, are under the management of the directors pending either liquidation, return to solvency, or the imposition of some alternative administration.'

...but, when is a company 'approaching insolvency'?

Insolvency

Common Law Duties

- Bona fide in the Company's best interests
- To avoid conflicts of interest

Consider

(1) Professional Directors; Fees to employer in arrears; Company becoming seriously short of cash, but asset rich; Do they pay their employer? Do they make any further distributions to the economic owner (who is a valued client)?

(2) Fund; Subsidiary; Parent as nominee investor; Solvency concerns. Do the directors' take account of investors interests (as they are required to do under the Pol Law, or creditors)?

Insolvency

Statutory Duties

Section 422 – Delinquent Officers:

- Where in the course of the winding up of a company it appears that any person (defined to include a director) ...has otherwise been guilty of any misfeasance or breach of fiduciary duty in relation to the company, the liquidator or any creditor or member of the company may apply to the Court for an order under this section.

Section 434 – Wrongful trading:

- Where the company has gone into insolvent liquidation and (1) 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 of the company avoiding going into insolvent liquidation, and (2) that person was a director of the company at that time and (3) the Director did not take every step with a view to minimising the potential loss to the company's creditors that (assuming him to have known that there was no reasonable prospect of the company avoiding going into insolvent liquidation) he ought to have taken.

Consequences

- Breach of fiduciary duty
 - Action brought by company against director(s) individually
 - Potential liability for negligence
 - Account to company for losses
- Winding up or insolvency
 - Liquidator may bring action against directors for losses to the company caused by the directors' negligence or breach of any duties owed to the company
- Fiduciaries, Insurance and Banking laws
 - Breach of codes of practice admissible in evidence in legal proceedings

Consequences

- Disqualification:
 - Where by reason of conduct in relation to a company or otherwise a person is unfit to be concerned in the management of a company
 - Factors to determine fitness include:
 - Competence, experience, judgment; diligence; qualifications; misfeasance and breach of fiduciary duty
 - Applicant:
 - Commerce & Employment, GFSC, HM Procureur, Registrar, a company, insolvency officer, any other interested party
 - Maximum Period – 15 years

Relief from consequences

What might work...

- D&O insurance
 - Company may purchase and maintain insurance for directors against liability
- Ratification
 - Company may ratify director's negligence, breach of duty or breach of trust; but
 - (1) Bona fide and honest and (2) Not jeopardise solvency or cause loss to creditors: *Bowthorpe Holdings Ltd and another v Hills and others*

Relief from consequences

What won't work...

- Exclusion clauses for negligence, default, breach of duty or breach of trust
 - Provision exempting a director from liability in connection with any of the above is void
 - Any indemnity provided by the company in respect of liability for the above is void
 - Gross negligence

A moment to talk about the Code of Conduct

- Currently still in draft form
- An avalanche of responses – 3rd Party assessment and collation
- Awaiting further revision by the end of this year – early hint is that it will re-emerge as a less prescriptive document
- Will have some degree of industry specificity
- There will be a second consultation
- Collas Day's views?

The Code – Our thoughts

- Comply (or complain?) or Explain – Who decides, what criteria do they use, are their decisions reviewable?
- Hindsight generally – Should there be express protection for good faith commercial judgment – i.e. a business judgment defence?
- Use Immunity – Why ‘fess up if you will just use it against me?
- Self dealing – What if the articles let me?

Questions?

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