

The Companies Act 2006 introduces an easily accessible statutory statement of the general duties of directors where previously directors had to look to case law to find out what those duties were. Here we provide an overview of the changes and how they effect directors.



What Are The New Statutory General Duties Of Directors?

Briefly, the new statutory general duties set out in the Companies Act 2006 are:

1. to act within the company's constitution and only to exercise powers for the purposes for which they are conferred (section 171);
2. to act in the way that the director considers, in good faith, would be most likely to promote the success of the company for the benefit of its members (section 172);
3. to exercise independent judgment (section 173);
4. to exercise reasonable care and skill (section 174);
5. to avoid a situation in which the director has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company (section 175);
6. not to accept a benefit from a third party conferred by reason of the director being a director or the director doing (or not doing) anything as director (section 176); and
7. if the director is in any way, directly or indirectly, interested in a proposed transaction or arrangement with the company, to declare the nature and extent of that interest to the other directors (section 177).

The first four of these statutory general duties were brought into force on 1 October 2007. The remainder were originally expected to be brought into force on 1 October 2008, but this is the subject of consultation.

What Changes Do the Statutory General Duties Introduce?

The statutory general duties are mostly based on existing case law, although there are some subtle differences which may prove to be significant.

Enlightened Shareholder Value

One clear change is the introduction by section 172 of the concept of "enlightened shareholder value" – a term which the section itself does not use.

To discharge their duties under section 172 directors must have regard (among 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 suppliers, customers and others;

This briefing is for general information only and is not intended as a substitute for taking appropriate professional advice.

- the impact of the company's operations on the community and the environment;
- the desirability of the company maintaining a reputation of high standards of business conduct; and
- the need to act fairly as between the members of the company.

Even if directors already have regard to these factors in reaching their decisions, it may now be prudent to ensure that their board minutes document this fact adequately.

To Whom Are the Statutory General Duties Owed?

A director's statutory general duties are owed to the company (section 170(1) of the 2006 Act), not to the shareholders or to anyone else.

The Risk of Derivative Claims

Sections 260 to 264 do, however, permit a member of a company to bring a derivative claim: that is to say proceedings in respect of a cause of action vested in the company which seeks relief on behalf of the company.

This may allow a dissatisfied shareholder to bring proceedings against directors on behalf of the company. But such a shareholder would need the permission of the court to continue the claim and the court must refuse this if it considers that someone acting to promote the success of the company would not pursue the claim.

New Restriction on Member Ratification

Section 239 now effectively provides that a members' resolution to ratify the conduct of a director or former director amounting to negligence, default, breach of duty or breach of trust in relation to the company is only effective if it is passed by the necessary majority without counting any votes in its favour by the director or those connected with him.

This provision is likely to be of particular concern to directors whose majority shareholding had hitherto assured them of member ratification should they ever need it.

Conclusion

It should not be forgotten that, quite apart from the statutory general duties, there are many other statutory duties and liabilities on directors. These include, for example, those in relation to the preparation of reports and accounts, the filing of returns, the maintaining of minutes and registers, environmental and health and safety matters, and wrongful trading in the event of insolvency.

The purpose of the statutory general duties is to make what is expected of directors clearer and more accessible than the previous judge made law that the duties replace. But, the statutory general duties' occasional subtle departures from the case law on which they are based and the introduction of the concept of enlightened shareholder value may well, initially at least, introduce more uncertainty into the very area of the law that these duties seek to make clearer and more accessible.

November 2007

Offices

Westminster

Burwood House
14-16 Caxton Street
London SW1H 0QY
Tel: +44(0)20 7873 1000
Fax: +44(0)20 7873 1010

Ealing

55 Uxbridge Road
Ealing
London W5 5SA
Tel: +44(0)20 7873 1000
Fax: +44(0)20 8573 5352

Contact

Company Commercial
Nicholas Phillips
nicholas.phillips@williamsturges.co.uk

www.williamsturges.co.uk