

GOVERNANCE

Directors' Duties and Conflicts

The seven statutory duties in practice, and how to declare and manage conflicts of interest properly.

Duties owed to the company

Directors of a company registered in England and Wales owe general duties set out in the Companies Act 2006 (sections 171 to 177). They are owed to the company, not to individual shareholders, and they apply to every director, whether executive, non-executive or a family member appointed to the board. They can also apply to someone who acts as a director without being appointed.

The seven duties

1. **Act within powers.** Follow the articles and use powers only for the purpose they were given.
2. **Promote the success of the company.** Act in the way the director considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, with regard to employees, suppliers, customers, the community and the environment, and long-term consequences. Where the company is in financial difficulty, creditors' interests come into play.
3. **Exercise independent judgment.** A director may take advice but cannot simply follow a shareholder's wishes.
4. **Exercise reasonable care, skill and diligence.** The standard is that of a reasonably diligent person with the director's knowledge and experience, and at least the general knowledge expected of a director.
5. **Avoid conflicts of interest.** Do not put yourself in a position where your interests conflict, or may conflict, with the company's.
6. **Not accept benefits from third parties** given because of being a director or for doing, or not doing, something as a director.
7. **Declare an interest in a proposed transaction or arrangement** with the company.

In practice

In an owner-managed company the director is often also the shareholder, and the line between personal and company decisions is easy to blur. Using company money, taking an opportunity the company could have taken, or setting your own pay without a record are typical examples. The duties are easier to meet where decisions are minuted, reasons recorded and independent advice taken on significant matters.

Key points

- The duties are owed to the company, and apply to all directors.
- Conflicts must be declared and managed, not hidden.
- Record decisions and reasons in minutes.
- Some transactions need shareholder approval.
- Directors can be personally liable for breach.
- Review the board's practice each year.

Conflicts of interest

A conflict arises when a director has a personal interest that may compete with the company's: a contract with a company they own, a loan, a property sale, or a role with a competitor. The law deals with them in layers.

- **Declare.** A director must declare the nature and extent of an interest in a proposed transaction to the other directors before the company enters into it. An existing interest in a transaction already made must be declared too (sections 177 and 182).
- **Authorise.** For a private company, the other directors can authorise a conflict, if the articles do not prevent it, and the conflicted director does not count in the quorum or vote (section 175).
- **Record.** Minute the declaration, the decision and the reason.
- **Update.** Where the interest continues, such as an ongoing arrangement with a connected company, revisit it.

Before you start

- Who are all the directors?
- Does any have an interest in a company transaction?
- Is it declared and recorded?
- Are shareholders' approvals needed?
- Do the articles allow authorisation?
- When were the registers last reviewed?

Transactions needing shareholder approval

Some arrangements cannot be left to the board. Substantial property transactions between a company and a director or a connected person normally need approval by the members (section 190). Loans to directors have their own rules, and a loan that is not repaid may bring tax consequences for the company and the director. Long service contracts and payments for loss of office also need approval.

Keeping the evidence

Good governance is mostly good records. Hold board meetings, minute the decisions and keep the register of directors' interests. Check the register of directors, the confirmation statement and the register of people with significant control. Companies House can now verify directors' identity, which brings new filing duties.

When the company is in difficulty

When a company is insolvent, or likely to become so, directors must consider the interests of creditors, and personal liability can follow for wrongful trading, preferring one creditor over another, or continuing to trade when there is no reasonable prospect of avoiding insolvency. Take advice early from an insolvency practitioner or solicitor, and keep a clear record of decisions and the reasons for them.

How MTM can help

0161 835 2080
client@mtmlp.co.uk

We help companies keep proper records of directors' decisions, prepare board and shareholder approvals, update the statutory registers and make the Companies House filings. We can prepare a short conflicts policy and a register of interests for your client. Legal advice on a director's personal liability should come from a solicitor.