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## The Board of Directors: Authority, Duties and Breach

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Please note that this is a preliminary article and is no substitute for the taking of detailed legal advice. It highlights some of the main considerations which may apply.

### Delegation of Powers: The company's constitution

The company's constitution, otherwise known as the articles of association (the articles), makes important provision on the division of power of governance of the company between the board of directors (BoD) and the Shareholders' General Meeting (GM). Articles 3 & 4 of the Model Articles for Private Companies provides for the delegation of power between the two organs governing the company.

Article 3 on 'Directors' general authority' states that 'Subject to the articles, the directors are responsible for the management of the company's business, for which purpose they may exercise all the powers of the company. Article 4 on 'Shareholders' reserve power' states that '(1) The shareholders may, by special resolution, direct the directors to take, or refrain from taking, specified action. (2) No such special resolution invalidates anything which the directors have done before the passing of the resolution.'

### Directors' Duties: s 170 – 177 Companies Act 2006

Given the wide discretion and authority given to the BoD by the articles, combined with the fact that directors occupy a position of trust towards the company as a whole according to common law, the Companies Act 2006 provides for a set of distinct codified duties that are owed to the company. These are outlined below:

The Companies Act 2006 provides for seven (7) distinct duties:

- *Duty to act within powers* – a director must act within the powers permitted in the company's articles of association or otherwise approved by the company's members; **s 171 CA 2006**
- *Duty to promote the success of the Company* – a director must act in a way which he believes will most likely promote the success of the company for the benefit of all its shareholders. There are several factors which a director must consider in this regard; **s 172 CA 2006**
- *Duty to exercise independent judgement* – a director must make his own decisions and should not follow another person's directions unless they agree with it; **s 173 CA 2006**
- *Duty to exercise reasonable care, skill and diligence* – which duty is judged against both the actual knowledge, skill and experience of the director concerned and also against the standard reasonably expected of a director carrying out his functions; **s 174 CA 2006**
- *Duty to avoid conflicts of interest* – a director must avoid a situation where his duties to the company are conflicted with any other interests or duties he owes to a third party (unless otherwise authorised by the company); **s 175 CA 2006**

- *Duty not to accept benefits from third parties* – a director must not accept any benefit which is given because of his office as director or in consequence of him doing or not doing anything as a director; **s 176 CA 2006**
- *Duty to declare interests* – a director must declare his interest in any proposed transaction or arrangement with the company; **s 177 CA 2006**

### **Consequence of a Breach of Duty**

Section 178 of the Companies Act 2006 provides that a company can make the following claims in case of a breach. The Company can itself bring a claim against the erring director if it can show that it has suffered some loss and more specifically, if the director has made some personal profit, they can be required to surrender it to the company. Another consequence is that a contract or other arrangement entered into by the director in breach of duty may be void. Immediate options to consider include issuing an injunction to stop the director from carrying out or continuing with the breach (s 40(4) CA 2006) and requesting damages by way of compensation where the director has been negligent, as well as the rescinding of a contract in which the director has had an undisclosed interest.

It is important to note that shareholders can play a role when it comes to the ratification of certain transactions to be undertaken by the board of directors and the ratification of a breach of duty. A distinction exists between transactions requiring prior shareholder approval and processing shareholder approval of a given breach of a directors' duty towards the company. Transactions which according to the Companies Act 2006 require prior shareholder approval are outlined in Chapter 4 of the Companies Act 2006 (ss 180 CA 2006). Section 239 of the Companies Act 2006 and additional case law provide the legal background on which types of breaches are ratifiable and which not.

If a breach is not authorized by the process outlined in the Companies Act 2006, then shareholders have the option to proceed with a Derivative claim, whereby with the permission of the Court, the shareholders can bring a claim against a director, in the name of the company. Claims by the company itself against a company director who was in breach are often retrospective. These claims are either brought by members of the existing board against their predecessors, or by the new owners when the company is sold, who may appoint new directors that investigate past breaches of duty and the opportunity to hold the previous directors to account.