Information

KNOWLEDGE HUB

Directors - Duties, Responsibilities and Liabilities

The board of directors of a company is primarily responsible for:

- Determining the company's strategic objectives and policies.
- Monitoring progress towards achieving the objectives and policies.
- Appointing senior management.
- Accounting for the company's activities to relevant parties, eg shareholders.

The managing director/chief executive is responsible for the performance of the company, as dictated by the board's overall strategy. He or she reports to the chairman or board of directors.

Appointment

The first directors of a company are appointed at the time of its registration. Subsequent appointments are governed by the company's articles of association. Typically the articles will provide for the board of directors to fill any casual vacancies or to appoint additional directors up to the maximum number specified by the articles.

On appointment a new director will be asked to provide certain personal information (ie full name, address and any other directorships held) to be included in form 288(a) which he/she will be required to sign to signify consent to act as a director. The director will be reminded to acquire the share qualification (if any) specified in the articles. Additionally, the director will be required to disclose any interests in shares or debentures in the company and will be invited to give a general notice of any interests in contracts involving the company.

On a practical note the new director should make sure that he/she receives: a copy of the company's memorandum and articles of association; details of the business and affairs of the company, eg recent board minutes and management accounts; and the statutory reports and accounts for the past two years.

A director's service agreement

An executive director has certain rights and obligations arising as an employee as well as a director of a company. These should be outlined in a director's service agreement, which should include the following information:

- Appointment commencement date, employment commencement date (which may be different), notice required by either party to terminate the agreement and the normal retirement age which cannot be less than 65 unless objectively justified.
- Duties of the director including any provisions under which a director may be required to serve on the boards of companies within a group of companies.
- Limitations on the director in engaging in business or professional activities outside the employment, and method of obtaining prior approval if such activity might be acceptable to the company.
- Remuneration details: salary, bonus schemes, share options, medical insurance, life and disability insurance, pensions, company car and / or other benefits including sufficient flexibility for the company to review, amend or withdraw the benefit in appropriate circumstances.
- Details of reimbursement and authorisation for expenses.
- Location of the director's main place of work, arrangements relating to any future change of location on a permanent or temporary basis and details relating to the requirement to travel for business.
- Holiday entitlements.

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- Entitlements relating to pay during periods of absence due to sickness or accidents.
- The right for the company to require the director to undergo a reasonable medical examination and for the reports from such examinations to be disclosed to and discussed with the company.
- Provisions concerning disclosure of company information which is considered confidential.
- Provisions relating to intellectual property issues.
- Circumstances under which the service agreement may be terminated by the company without notice.
- Where the grievance, disciplinary and appeals procedures may be found (the procedures themselves normally being non-contractual).
- Details of any constraints that may apply to the director on leaving the company including working for a competing organisation, setting up in competition to the company, soliciting or dealing with company clients and poaching senior members of staff.
- Other provisions relating to the termination of the employment including the right for the company to give pay in lieu of notice and/or to place the director on gardening leave and the return of company property.
- Specification of which law governs the agreement (eg the law of England).
- Evidence that the agreement has been approved by the board.

Powers

The directors are generally responsible for the management of the company and they may exercise all the powers of the company. However, the extent of their authority may be constrained by the Companies Act and the articles of association. For example, articles of association often include provisions and restrictions on borrowing by the company.

Generally, the directors must act collectively as a board to bind the company. However, the articles usually entitle the board to delegate powers to individual directors as considered appropriate. In practice individual directors will normally carry out many of the company's activities.

Duties

Statutory duties

- A director must not put himself in a position where the interests of the company conflict with his personal interest or his duty to a third party.
- A director must not make a personal profit out of his position as a director unless he/she is permitted to do so by the company.
- A director must act bona fide in what he/she considers is in the interests of the company as a whole, and not for any collateral purpose.

Many of the duties and obligations of a director are mandated by the Companies Act 2006. Others are governed by the Insolvency Act 1986 and the Company Directors' Disqualification Act 1986.

Directors are responsible for making sure that the company fulfils its statutory duties. Generally, the company secretary will be responsible for the performance of most of the duties imposed by the Companies Act. Consequently, the directors should ensure that the secretary is competent to discharge those duties properly.

Directors may be liable to penalties if the company fails to carry out its statutory duties. However, they may have a defence if they had reasonable grounds to believe that a competent person had been given the duty seeing that the statutory provisions were complied with.

The main statutory responsibility falling on directors is the preparation of the accounts and the report of the directors. It is the responsibility of the directors to ensure that the company maintains full and accurate accounting records. This includes the preparation of a balance sheet and a profit and loss account for each financial period of the company, and the presentation of these to shareholders and, subject to various exemptions, the filing of the accounts and report of the directors with the Registrar of Companies.

In addition to the above, on an individual level, directors have a responsibility to disclose to the board their interests in dealings with the company, in particular in respect of the following:

- An interest in a contract with the company.
- Interests in shares or debentures of the company.
- Dealings in options of the shares of the company.

Duty of skill and care

Directors are expected to display a certain amount of skill and exercise reasonable care in the performance of their work.

Liabilities

Directors may incur personal liability, both civil and criminal, for their acts or omissions in directing the company.

It is beyond the scope of this paper to list all the various matters for which directors can be held to be liable. However, directors should be aware of the effects of the Company Directors' Disqualification Act 1986, which could lead to the disqualification from acting as a director of a company for a period of between two and 15 years, and the Insolvency Act 1986 which gives rise to the possibility of directors being made personally liable for the company's debts, the Health and Safety at Work etc Act 1974, and the Corporate Manslaughter and Corporate Homicide Act 2007.

Company Directors' Disqualification Act 1986

The circumstances in which an application may be made for the disqualification of a director are as follows:

- The director has been guilty of three or more defaults in complying with companies legislation regarding the filing of documents with the Registrar of Companies during the preceding five years.
- He or she is, or was, a director of a company that has at any time become insolvent and that his/her conduct as a director of that company makes him/her unfit to be concerned in the management of a company.
- The director is found to be guilty of wrongful or fraudulent trading as defined in the Insolvency Act 1986 (see below).

Insolvency Act 1986

Wrongful trading

If a company has gone into insolvent liquidation and before that liquidation took place a director knew, or ought to have known, that there was no reasonable prospect that the company could avoid the liquidation, then the court may declare that the director make a personal contribution to the company's assets.

However, the director will not be made personally liable in circumstances where he/she can show that he/she took every step prior to the liquidation to minimise the potential loss to the company's creditors.

Fraudulent trading

Under this heading the court may also require a director to make a contribution to the company's assets if, in the course of the winding up of a company, a director was knowingly a party to the carrying on of the company's business with the intent to defraud the creditors.

Health and Safety at Work etc Act 1974

Health and safety law places duties on organisations and employers, and directors can be personally liable when these duties are breached: members of the board have both collective and individual responsibility for health and safety. Larger public and private sector organisations need to have formal procedures for auditing and reporting health and safety performance.

If a health and safety offence is committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other similar officer of the organisation, then that person (as well as the organisation) can be prosecuted under section 37 of the Health and Safety at Work etc Act 1974.

Those found guilty are liable for fines and, in some cases, imprisonment. In addition, the Company Directors Disqualification Act 1986, section 2(1), empowers the court to disqualify an individual convicted of an offence in connection with the management of a company. This includes health and safety offences. This power is exercised at the discretion of the court; it requires no additional investigation or evidence.

Individual directors are also potentially liable for other related offences, such as the common law offence of gross negligence manslaughter. Under the common law, gross negligence manslaughter is proved when individual officers of a company (directors or business owners) by their own grossly negligent behaviour cause death. This offence is punishable by a maximum of life imprisonment.

Note: equivalent legislation exists in Northern Ireland, ie article 34A of the Health and Safety at Work (Northern Ireland) Order 1978 and article 3(1) of the Company Directors Disqualification (Northern Ireland) Order 2002.

Corporate Manslaughter and Corporate Homicide Act 2007

Under this Act, an offence will be committed where failings by an organisation's senior management are a substantial element in any gross breach of the duty of care owed to the organisation's employees or members of the public, which results in death. The maximum penalty is an unlimited fine and the court can additionally make a publicity order requiring the organisation to publish details of its conviction and fine.

Further information and guidance is available at www.iod.com/hsguide

Recommendation

This paper is only a brief summary of the duties, responsibilities and liabilities an individual will assume on being appointed a director of a company. On such first appointment it is strongly recommended that more detailed information is obtained. In larger companies, however, the company secretary will be able to give appropriate guidance.

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