



The duties that directors have to perform are one of the most important aspects of company administration. Directors (and the company secretary (if there is one)) must be aware of. This Guide explains these duties in light of the Companies Act 2006 (most particularly concerning directors, including their duties, directors' remuneration, loans to directors, shareholder litigation and insurance).

Directors' Duties

The board of directors has control over the management of a company's business. They make the strategic decisions of a company.

Prior to 1st October 2008, the duties of directors were derived from several sources, including the common law, the Companies Act 1985 and other statutes.

Following the introduction of the Companies Act 2006, directors' common law duties were codified in a statutory statement of duties set out in sections 171-177 of the Companies Act 2006. However it would be wrong to say that the provisions of the Act in this area not only codify the more fundamental aspects of the common law on directors' duties but develop them further.

These duties apply to executive directors (and shadow directors). The duties are owed to the company. A director for breach of duty (and the company's shareholders can bring a derivative action on the company's behalf, see below).

The general duties under the Companies Act 2006 are as follows:

- **Act within powers.** A director must exercise powers only in accordance with the company's constitution and the powers conferred on them (section 171).

The company's constitution includes the company's articles of association, resolutions and agreements of a constitution (including shareholder agreements).

- **Promote the success of the company.** In other words, a director must act in a way that he or she believes to be most likely to promote the success of the company as a whole (section 172).

(This section 172 duty is subject to the provisions that directors must act in good faith in the course of making their decisions. There is a number of likely consequences of the duty to promote the success of the company, including: the need to consider the interests of the company's employees; the need to consider the interests of the company's customers and others; the need to consider the interests of the community and the environment; the need to consider the company's reputation for high standards of business conduct.)

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standards of business conduct (section 172 of the Companies Act 2006 (the company).)

- **Exercise independent judgment** (section 173).

This would not prevent a director from acting in accordance with the company's constitution or an agreement entered into.

- **Exercise reasonable care, skill and diligence** (section 174).

The expected standard is that of a reasonably diligent person in the same position. A director's actual understanding may not be enough if more could reasonably be expected.

- **Avoid conflicts of interest** (section 175).

Directors must avoid situations where they have, or could have, a conflict of interest with the company. This applies in particular to the exploitation of any opportunity regardless of whether or not the company could take it.

- **Not accept benefits from company** (section 176). A director or a company must not make a personal profit from the position of director or a company, except where authorised to do so by the company (section 176).

- **Declare interests in proposed transactions or arrangements with the company.** A duty to disclose the company (section 177).

Any director, directly or indirectly, who is or has been involved in a transaction or arrangement with the company must declare the interest to the other directors.

The statement of general duties is a statement of the way directors are expected to act and for how they account to the company.

Duties owed to the Company

These general duties are owed to the company, not the individual shareholders. As described above, it is the company that can bring an action against a director for breach of duty. A breach of duty means a director concerned and allows the company to claim damages or compensation from the director concerned and allows the company to claim an injunction as well. Failure to disclose an interest in an existing transaction or arrangement with the company also carries the risk of criminal fine.

Shareholder Litigation and Derivative Claims

However notwithstanding that the Companies Act 2006 allows shareholders to bring an action against a director in the company's name (known as a "derivative claim") for a loss arising from an actual or proposed act or omission of a director of the company, default, breach of duty or breach of trust by a director of the company.

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However, it is only the compa derivative claim. In addition, th must go through, including cou sue. It is not therefore a straig need to approach with caution. those without any real merit.

Ratification

If a director commits negligenc can ratify the breach by passin shareholder, any votes he or sh family or other 'connected pe whether a simple majority has unanimous.

Conflicts of Interest

Company secretaries and com about conflicts of interests. Th duties specified under the Cor follows:

- **Section 175** - A duty proposed transaction
- **Section 176** - A duty
- **Section 177** - A d transaction or arrang

Duty to avoid conflicts of interest

A **conflict of interest** occurs interests, one of which could po A conflict of private interest aris be perceived as being capable

For example, suppose the boa property. One of the directors increase in value subsequent to of interest, as his judgement m neighbouring property rise in va

Other potential conflict situation company (e.g. an accountant to to a person who is or may be in

Prior authorisation by the board

not matter whether the loss occurred hne the derivative claim became a

who may obtain compensation in a o an action and criteria that the claim eholder is actually able to proceed to one that potential shareholders will ect directors from spurious claims or

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ould be prepared to advise directors as three out of the seven directors' ern conflicts of interest. They are as

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organisation) is involved in multiple tion for an act in relation to the other. any interest which *might* influence, or udgement even unconsciously.

any is discussing an investment in a property, which has the potential to company. That director has a conflict sire to see his own investment in his

ctorships, advisory positions with the director as well) and being connected

A conflict situation can potentially arise where a director's duty is not infringed.

- the matter has been authorised by the board of directors;
- the director is not connected with the matter; and
- the matter is agreed by the independent non-executive directors.

For companies incorporated since 1 October 2009:

The company's articles must be consistent with the provisions that could invalidate an authorisation.

For companies that were in existence on 1 October 2009:

The shareholders should pass a resolution enabling the board to authorise conflicts, (See: [Shareholders' Conflicts of Interest](#)). This resolution then needs to be passed by the Companies House – File Resolution.

The interested director must consider the matter with a view to the company's interests, not his own. An existing or proposed transaction.

- at a meeting of the board of directors; or
- by notice in writing, (See: [Declaration of Director's Interest in Proposed Transaction](#)); or
- by general notice, (See: [General Notice of a Director's Interests](#)).

Often a director will take advantage of his position to give a general notice of interest to a person connected with him. Such a notice should always be recorded in the minutes.

Even once the board has authorised a transaction, the director concerned is still under a duty to act in a way that he or she is likely to promote the success of the company (section 172 duty).

Where a director is not aware of a transaction or arrangement in connection with the company, the director is treated as being aware.

Considerations for the board

When the board considers whether to authorise a transaction, each director must consider the duty to act in a way that he or she is most likely to promote the company's interests.

The board may also want to inquire whether the director in question may not be able to discuss the matter.

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and the meeting at which the matter is considered. The director is not to cast any vote cast by the interested director.

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For 2008:

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his interest, to enable the board to consider the matter with a view to the company's interests. The declaration in relation to either an existing or proposed transaction must be made in one of three ways:

- at a meeting of the board of directors; or
- by notice in writing, (See: [Declaration of Director's Interest in Proposed Transaction](#)); or
- by general notice, (See: [General Notice of a Director's Interests](#)).

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Some situations where a declaration of interest is advisable

There are several situations where a director may need to declare a conflict of interest.

For example:

- Where a director sits on or holds shares in a company or directorships authorised by the company
- Where a director holds shares in a potentially competing company.
- Where a director owns or has an interest in the company's property, or the value of the company's activities.
- Where a director has a business relationship with the company, or an interest in a business or company – for example, accountants, legal or consultancy.

Situations where there is no need to declare a conflict of interest

A director need not declare an interest in the following circumstances:

- if it cannot reasonably be expected that the director's interest will give rise to a conflict of interest; or
- if the other directors are aware of the interest and for this purpose the other directors are treated as being aware; or
- if it concerns terms of a contract that have been or are to be considered by a meeting of the directors.

Who are connected persons

Connected persons include the following:

- Family members (spouse, children and step-children, anybody with whom the director lives in the same household, 'relationship', parents)
- Trustees of a trust of which the director or a family member, is a beneficiary
- Corporate bodies to which the director or a family member, is a beneficiary
- A director's business partner

'Connected persons' interests also fall under the remit of section 177 of the Companies Act 2006.

For example, if a director's spouse or child is a director of a potentially competing business, a potential conflict of interest may arise. A declaration of his indirect interest must be made, and the board should give prior authorisation for the purchase, and the board should consider it does not interfere with their duty as directors.

Substantial property transactions

A substantial property transaction is defined as the sale or disposal of non-cash assets to or from directors or connected persons. There are restrictions in the Companies Act 2006 to prevent a company from transferring substantial assets from or to

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directors of the company, or from the company, unless the consent is obtained.

Shareholder approval is required if the asset being transferred is either:

- more than £100,000,
- more than 10% of the value of the company's assets (as shown in the company accounts), or

(See: [Shareholders' Approval of Substantial Property Transaction](#)).

Payments under directors' service contracts are excluded from the scope of the substantial property transaction provisions where an acquisition or disposal is made in the capacity as a shareholder of the company.

Members' approval is also not required if the transaction is pursuant to a members' voluntary arrangement (note, however, that the requirement for approval remains in force if the company is in receivership or administrative liquidation).

Proceedings of Directors

Under both Table A (Companies Act 2006) and the Model Articles, decisions can be made by the directors by a majority vote in a meeting, or unanimously in writing. Under Table A - the directors are able to make decisions when not all of them are physically present, provided that they can communicate with each other (for example, by telephone or video conference).

Under both Table A and the Model Articles, the directors may appoint one or more directors, but the quorum may be reduced to one for companies with one director, the quorum for a meeting of directors is any two directors.

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Remuneration, Expenses, and Indemnification

Article 82 of Table A and article 82 of the Model Articles both state that directors are entitled to remuneration. Table A states that the level of remuneration is decided by the passing of an ordinary resolution of the shareholders, while the Model Articles permit the other directors to determine the level of remuneration.

Under the Model Articles, a director is entitled to receive remuneration not only for his services as a director but for any other services he may perform for the company. In both cases, the remuneration is deemed to accrue to the director in the absence of any provision to the contrary.

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Article 83 of Table A and article 87 of Table A both state that directors may be paid for out of pocket expenses in the discharge of their duties.

Article 87 of Table A and article 83 of Table A both allow directors to receive gratuities and pensions. Table A states that a director *no longer holds any executive office* with the company, whereas the Model Articles state that gratuities are included as part of a director's remuneration.

Note that if a director's service contract provides for a guaranteed term of more than two years, prior approval by way of resolution is required.

Loans to Directors

Loans to directors and the Companies Act 2006

The Companies Act 2006 removed the requirement for a company to obtain shareholder approval on loans to directors, replacing it instead with a requirement for loans to be subject to shareholder approval.

A private company may make a loan to a director, or give a guarantee or provide security in connection with a loan to a director, if the transaction must first be approved by a resolution of the shareholders, (See: [Shareholders' Ordinary Resolution for a Director](#)).

Exception for loans under s.115

If the aggregate value of the loans to a director does not exceed £10,000, there is no need to obtain shareholder approval (note that the £10,000 is an aggregate value, meaning that if several loans to a director combine to a value over £10,000, it would require shareholder approval).

Other exceptions to the requirement for shareholder approval

There are other exceptions to the requirement for shareholder approval. For example, where the loan or expenditure (of under £50,000) on behalf of a director with funds to defend civil or criminal proceedings in connection with the company business, or where the loan or expenditure is for the purposes of the company business, or where the loan or expenditure is for the purposes of the company business, or where the loan or expenditure is for the purposes of the company business.

Note 'connected persons'

Companies should watch out for transactions with a director requires shareholder approval will also be required in respect of a transaction *between the company and a connected person*.

Thus a loan to a 'connected person' requires shareholder approval.

Connected persons include the following:

- Members of the director's family (including civil partner, live-in partner, children or step children, children of a civil partner, live-in partner, and parents).

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- A company in which the director exercises more than 20% of the share capital, or can exercise more than 20% of the share capital.
- A trustee, where the director is a trustee of the trust.
- A partner of the director, where the director is a partner connected with the director.
- A legal firm where the director is a partner, where a connected person is a partner.

Practical steps for approval

In practical terms;

1. The first step is to call a general meeting. [Board Minutes – Consider Director's Loan and Call General Meeting](#)
 - a. A declaration of interest must be made by the director requesting a loan (note the 'disinterested interests' of the director, where the director is not the director above).
 - b. Discuss the proposed loan. If the loan is less than £10,000, shareholder approval is not required. If the loan is more than £10,000, the loan will need board approval. When approving such a loan, the board should be mindful of their duties; the board should only approve the loan if it will *promote the success of the company*.
 - c. If the board approves the loan, a memorandum must be prepared, setting out the terms of the memorandum, the nature and purpose of the loan.
 - The nature of the transaction
 - The amount of the loan
 - The extent of the company's liability
 - d. Resolve to call a general meeting to seek a shareholders' written resolution.
2. Secondly, the memorandum must be made available to shareholders by being sent to them. The general meeting is to be held, being made available before the general meeting and at the general meeting itself.
3. Finally, hold the general meeting to seek the shareholders' approval. Then arrange for the execution of the loan agreement. The loan agreement should have been approved at the previous general meeting.

Simply Docs Loan Agreement

Simply-docs offers three templates for a loan agreement over joint property. These are s

The secured loans grant the company a weaker form of security than a charge. We also provide guidance on the company's equitable charge

– unsecured, secured and secured with a charge. See [Directors' Loan Agreements](#).

charge over the director's home. This is a Land Registry formality. The Land Registry formalities are simpler. The conditions that need to be made to protect

Consumer Credit Act

The company should ensure that the loan is either by complying with the requirements of one of the exemptions. Information is available on the Office of Fair Trading website at <http://www.offt.gov.uk>.

Loans from Directors' to a Company

A director (or shareholder) can make a loan to the company if the organisation makes a loan to the director for the requirements, particularly if the loan is for the requirements of a director may make the loan to the company, this will particularly if the director is the sole director and sole shareholder of the company will need to include conditions precedent, representations and warranties.

Whether the director will require to pay interest on the loan is a commercial matter. However, the director should consider their own personal tax position and may need to consult a tax advisor and consult HMRC.

A loan from a director to a company will need to satisfy the requirements of the Companies Act 2006 (section 177) – see above. If the lender is a director of the borrower, that director must declare the nature of his interest in the transaction under section 177 of the Companies Act (again see above). The director must abstain from voting on the resolution to approve the loan.

Our loan and finance documents should be drafted to reflect the above. A director seeking to make a loan to the company should consider the above.

Indemnity and Insurance

Under the 2006 Act, a company can indemnify a director from any liability for negligence, default, breach of duty or breach of trust in connection with the company. Any attempt to do is void.

However, this does not prevent a company from purchasing insurance for its directors against such negligence, default, breach of duty or breach of trust. The purchase of such insurance must be authorised either by the articles or by a resolution of the shareholders (or by the directors if there is no equivalent provision in the articles).

Any loan made by the company must comply with the Consumer Credit Act 1974, which requires the company to ensure that the loan is either by complying with the requirements of one of the exemptions, including licensing and exemptions, is available on the Office of Fair Trading website at <http://www.offt.gov.uk>.

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