



# CORPORATE GUIDE: THE DUTIES AND RESPONSIBILITIES OF A COMPANY DIRECTOR

This guide provides directors of UK incorporated companies with a general overview of the statutory and other duties and obligations which should be complied with in that role.

Additional duties will be applicable to directors of listed companies and directors of companies operating within regulated industries such as financial services, energy or insurance. While this guide does not address those additional obligations, instead being restricted to the issues of concern to most entrepreneurs, we would be happy to advise.

If, having considered this guide, you would like to know more or to discuss your own circumstances in greater detail, please speak to your usual contact at Stevens & Bolton or a contact listed at the end of this guide.

## WHAT IS THE ROLE OF A DIRECTOR?

Each individual director should participate regularly in board meetings to assist the board in taking decisions and meeting the company's obligations.

The board of directors of a UK company is responsible for day to day strategic and operational management of the company's business, including responsibility for ensuring that the company meets its statutory and other legal obligations. The board of directors is entirely separate from the shareholders of the company, even though there may be considerable overlap between the individuals concerned. Unless given additional special rights through the articles of association or contractually, shareholders only take decisions in a limited number of areas where the law (particularly the Companies Act 2006) provides for shareholder approval.

Each individual director should participate regularly in board meetings to assist the board in taking decisions and meeting the company's obligations. Although individual directors may have particular responsibilities or specialist roles (e.g. finance director, sales director), as a general principle all directors are equally responsible for all actions of the board. However, the board is usually permitted to delegate certain of its powers to committees of the board or to individual directors or employees.

## STATUTORY GENERAL DUTIES UNDER THE COMPANIES ACT 2006

There are seven statutory duties under the Companies Act 2006:

### 1. To promote the success of the company

This requires a director to act in the way he or she considers, in good faith, would most likely to promote the success of the company for the benefit of its members as a whole.

While it is for the directors themselves to decide, in good faith, whether a particular course of action is likely to promote the success of the company, a non-exhaustive list of factors which each director should consider has been provided – the Companies Act 2006 states that a director should have regard to:

Directors of subsidiary companies should remember that the exercise of their duties should have regard to the position of the subsidiary company itself.

- the likely consequences of any decision in the long-term;
- the interests of employees of the company;
- the need to foster business relationships with suppliers, customers and others;
- the impact of the company's operations on the community and environment;
- the desirability of the company maintaining a reputation for high standards of business conduct; and
- the need to act fairly as between members of the company.

In practice, these factors will rarely all be relevant to a particular decision, and as mentioned they are not exhaustive - if directors act in good faith, the courts are unlikely to question their judgment as long as they are seen to be operating in a responsible manner.

### 2. To act within its powers

i.e. in accordance with the company's constitution (including the articles of association).

### 3. To exercise independent judgment

All directors are expected to exercise independent judgment and make their own decisions in the particular circumstances. It should be noted that this requirement does not prevent the directors from complying with the company's constitution (see the duty in the preceding paragraph above) or from acting in accordance with an agreement the company has entered into.

Directors of subsidiary companies should remember that the exercise of their duties should have regard to the position of the subsidiary company itself, although the articles of association of the subsidiary may expressly require its directors to take into account the parent company's interests.

### 4. To exercise reasonable skill, care and diligence

This is a partly objective and partly subjective test. The standard required is the care, skill and diligence that would be exercised by a reasonably diligent person with:

- the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company (i.e. objective test); and
- the general knowledge, skill and experience that the director actually has (i.e. subjective test).

In practice, this means that where a director has a higher level of specialist knowledge and experience, he will be expected to perform to that higher level. However, it will not be possible to hide behind a lack of knowledge which the director should reasonably be expected to have, for example in relation to financial issues.

These duties are owed to the company and not to other group companies or individual shareholders.

**5. To declare interests in proposed or existing transactions or arrangements with the company**

Where a director has any direct or indirect interest in a transaction or arrangement with the company, he or she must declare that interest to the board – subject to anything to the contrary in the company’s articles of association, the board is not required to approve the interest, it must simply be declared. An example of such an interest is where a company is proposing to enter into a customer or supply contract with another company and a director is a director of both companies.

However, there is no need to disclose an interest:

- which cannot easily be regarded as likely to give rise to a conflict;
- to the extent that the other directors are aware (or ought reasonably to be aware) of it; or
- to the extent that it concerns his service contract with the company.

Where any such interest is declared, the ability for the director to vote and count in quorum of any board decision relating to the transaction or arrangement will depend on the articles of association – in many cases the director will be able to vote as long as he or she has complied with his obligation to declare the interest.

**6. Not to accept benefits from third parties**

This duty prevents a director from accepting a benefit from a third party which is given either because he or she is a director or because he or she does (or does not do) anything as a director. This includes non-financial as well as financial benefits, but only extends to benefits which can reasonably be regarded as likely to give rise to a conflict of interest.

This duty could be infringed by a director receiving lavish corporate hospitality – although it will obviously be a question of fact and degree as to whether the receipt of such benefit could be likely to give rise to a conflict.

**7. To avoid conflicts of interest**

This is a wider general duty to avoid conflicts – that is, a situation in which the director has or could have an interest that conflicts, or may conflict with the interests of the company.

An example of such “situational conflicts” is a director of company A also sitting on the board of company B, which is a potential competitor of company A.

Under the Companies Act 2006, a company is able to empower its directors to authorise such situational conflicts (before this legislation shareholder approval was required). Many companies have already taken the opportunity to empower their directors to authorise conflicts, through appropriate provisions being inserted into the company’s articles of association. In relation to approval of any conflict by the directors, the conflicted director and any other interested director is not entitled to vote or count in the quorum and it is not possible to override this provision by amending the articles of association.

**CONSEQUENCES OF BREACH OF GENERAL STATUTORY DUTIES**

These duties are owed to the company and not to other group companies or individual shareholders, so in most cases it’s the company that would take any action against an individual director. However, (i) in an insolvency situation a liquidator may take action and (ii) in certain limited circumstances it may be possible for a shareholder or group of shareholders to bring a “derivative action” against a director on behalf of the company.

Depending on the nature of the breach, a number of potential remedies could be available to claimants, including:

- the transaction being voidable (resulting in rescission of a contract or restoration of property);
- the payment of compensation or damages;
- a requirement to account for profits made;
- injunction;
- possible fines (e.g. failure to disclose an interest in an existing transaction or arrangement gives rise to criminal fines).

Most types of breaches are ratifiable by the shareholders, but some are not – for instance, where the director’s act is unlawful. However, in any shareholders’ decision to ratify, the vote of the director in breach, if he is a shareholder, will be discounted.

In certain circumstances, the court may also relieve a director from liability if it considers that he or she has “acted honestly and reasonably and, having regard to all the circumstances, ought fairly to be excused”.

The company may also have arranged insurance for the benefit of directors and/or be prepared to offer to assist the director by indemnifying him or her against costs incurred in successfully defending a claim for breach of duty owed to the company.

As soon as directors consider that their company may be getting into financial difficulties, they should seek independent advice.

## OTHER DUTIES AND RESPONSIBILITIES OF DIRECTORS

Directors have a range of other specific duties imposed by the companies’ legislation and other statutory or common law. Examples include:

- a range of administrative requirements relating to preparation and filing of annual reports and accounts and other publicity requirements;
- duties of confidentiality to the company, including only using or disclosing the company’s confidential information for the benefit of the company and its business;
- other statutory duties, for example relating to health and safety, anti-bribery/corruption and environmental legislation.

## WHAT IF THE COMPANY MIGHT BE GETTING INTO FINANCIAL DIFFICULTIES?

As soon as directors consider that their company may be getting into financial difficulties, they should seek independent advice. This is a point at which potential personal liability for the directors becomes a real risk, along with the prospect of being disqualified from acting as a director or being involved in the promotion or management of a company for many years. The best way to minimise these risks is to seek early professional advice.

Detailed guidance on these issues is beyond the scope of this guide, but please see our separate guide “Managing Financial Difficulty”.

## AND SO TO CONCLUDE...

Directors of UK companies have many duties and responsibilities which can make the role appear very onerous. While these duties and responsibilities should be taken very seriously, it should be remembered that as long as directors act honestly and in good faith and put steps in place to ensure that the company complies with its administrative and procedural obligations, personal liability for directors is rare, even in respect of companies that become insolvent.

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## KEY CONTACTS

For further information about any of the issues raised in this guide, please contact:



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