

Directors Conflicts:

Staying on the right side of the line

Directors' conflicts: staying on the right side of the line

Directors who are contemplating a move have to tread a careful path. They owe fiduciary duties to their company, which they must be careful not to breach, at the same time as they may be progressing plans for their new venture. We give some practical tips and hints based on recent case law that should assist directors in making the right decisions.

In a 2016 case, *Gamatronic (UK) Ltd v Hamilton [2016] EWHC 2225 (QB)*, H and M were director/shareholders and employees of Gamatronic. They were offered an opportunity to join Vox Ratio Limited ("Vox) to take up following departure from Gamatronic. There followed a series of actions taken by H and M which, following resignation, were alleged by Gamatronic to have comprised breaches of the directors' fiduciary duties. Amongst other remedies, Gamatronic sought an account of profits by way of compensation and also forfeiture and repayment of salaries paid during the period of alleged breach of duties.

Which duties were alleged to have been breached?

In *Gamatronic*, as in most cases with similar facts, the relevant directors' duties were:

- duty to act in good faith and promote the success of Gamatronic for the benefit of its members as a whole;
- duty to avoid a situation in which their interests directly or indirectly conflict with Gamatronic; and
- duty to disclose to the other directors of Gamatronic the nature and extent of any direct or indirect interest in any proposed transaction or arrangement with Gamatronic.

Preparatory steps

The cases show that mere "preparatory steps" to leave are not enough to be in breach of duty. But how to assess what the courts will class as "preparatory steps"? Clearly, the description of steps as merely "preparatory" will not be enough, and the judge in *Gamatronic* stressed that whether or not the acts said to be preparatory amount to a breach of any of the fiduciary duties in question is a highly fact-sensitive question.

What crossed the line into breach of duties territory in *Gamatronic*?

- helping Vox to create a price list (given that the pricing strategy of Gamatronic was clearly sensitive information and Vox was a potential competitor);
- taking a trip to the USA to advance Vox's business and taking steps to conceal the real reason for the trip;
- purchasing shares in Vox in the name of nominees;
- being actively involved, even to a limited extent, in Vox's operational matters; and
- continuing to engage Vox's services for Gamatronic's business.

What might have helped the directors?

The clear theme from the cases, including *Gamatronic*, is that full disclosure should be made to the company if a director is thinking of resigning to join a competitor. Some of the steps taken above crossed the line into breach of duty precisely because there was no disclosure and (for the USA trip) misleading reasons given for the time off. The point of disclosure is that it gives the company an opportunity to put rules in place regarding conflicts of interest.

The cost of crossing the line

In *Gamatronic*, H and M were held to be in breach of their duties but were not required to repay their salaries as it was held there was no reasonable relationship between the salaries and the breaches of duty and it would be inequitable to require them to do so. The amount of time spent on Vox matters was quite limited. A claim for an account of profits made by Vox to be returned to the company was also rejected on the basis that those profits had to bear a reasonable relationship to the breach of duty. This was not the case as there was a significant time gap between the last of the directors' breaches as fiduciaries and the profits claimed.

In this case, the company was not able to recover anything from the directors in respect of their breaches of duty. Nevertheless, *Gamatronic* is a useful reminder of the case law in this area and of the types of actions that will most likely be found to be in breach of duty. The message to any director thinking of resigning to join a competitor must be to:

- ask whether in his or her genuine opinion, in good faith, it would be in the company's interests to know of the plans;
- if yes, disclosure should be made to the company, since it is only on disclosure that the other directors can then take steps to protect the company's business.

This information is necessarily brief and is not intended to be an exhaustive statement of the law. It is essential that professional advice is sought before any decision is taken.

© *Stevens & Bolton LLP February 2017*



www.stevens-bolton.com

