

Directors' Duties – Traps for the Unwary

The recent Court of Appeal judgment in *Towers v Premier Waste Management Limited* is an example of the potentially harsh and onerous way in which directors' duties can apply in practice, and serves as a warning to those who regard them as solely of academic interest.

The Facts

Mr Towers was a director of Premier Waste Management Limited ("Premier"). Although he was not directly involved in the negotiation of the arrangement, he enjoyed a free, undisclosed and unapproved loan of equipment from a customer of Premier.

Although the equipment was in a relatively dilapidated state and Mr Towers only used it for a limited period of a few months, the equipment was located on his premises for several years. Furthermore, whilst on his premises it was also repaired at the cost of Premier.

A dispute arose when the customer tried to claim a hire charge from Premier for the period in respect of which the equipment had been loaned to Mr Towers. Although the claim between Premier and its customer was settled, Premier then sought to recover sums from Mr Towers.

The Consequences

Premier was trying to recover sums from Mr Towers on the basis that he had breached a number of his duties to the company as a director. Historically, these duties were set out in principles developed through case law, but recently have been codified in the Companies Act 2006. Previous decisions are however still relevant for assessing the implementation and effect of the "new" statutory directors' duties.

The most relevant statutory duties in this case were the general duty to promote the success of the company, the duty to avoid conflicts of interest and the duty not to accept benefits from third parties.

It has long been a settled principle of the case law in this area that a director can breach his duties to the company without having any fraudulent or dishonest intent, and whether or not the company suffers any loss as a result of the breach.

The sums involved in this case were relatively small, and indeed the judge commented that he was surprised that this had been allowed to proceed as far as it had. Premier had initially issued proceedings to recover £48,525 from Mr Towers, but Mr Towers was appealing against an order that he pay £7,997.31 (including interest).

The Court of Appeal upheld the original decision and rejected Mr Towers' appeal. The court rejected any arguments based on the fact that this type of transaction represented everyday

“commercial reality” or that any breaches of duty were so minor as to be unimportant. It focussed instead on the fact that Mr Towers had received a benefit which had not been disclosed to the company, and that there was a conflict of interest as a result given that Mr Towers was in a position to approve Premier’s transactions with the relevant customer (and indeed had done so in the past).

The Lesson

All directors of companies registered in England and Wales should be aware of their duties as a director. Unfortunately many are not, and even those who are often tend to regard those duties as esoteric legal rules which are unlikely to apply to them in practice, particularly where they act in good faith.

However, the risk of liability for breaching directors' duties is a real one. Even in an owner managed business where a director has control of shareholder votes, where the risk of any liability arising is relatively remote in the short term, the picture can change dramatically if, for example, there is a sale of shares, new directors are appointed who fall out with the other director or the company goes into administration/insolvent liquidation.

The *Towers* case highlights that even after the Companies Act 2006, the courts are willing to follow the historic strict approach to the application of these duties and factors such as absence of dishonest intent and absence of loss to the company will not necessarily be relevant in deciding whether or not a director is subject to liability under these provisions.

Although the principles behind these duties are fairly clear, the rules themselves can be complicated and difficult to apply, particularly in a joint venture company or group structure. As a general rule most breaches or potential breaches can be remedied by obtaining the informed prior consent of all relevant parties, but in practice of course this may be easier said than done. Certainly any directors who are concerned about these issues should consider taking advice as to how best to proceed, as given the strict application of these rules if a claim does arise ignorance of the law or lack of dishonesty are unlikely to be enough in themselves to prevent liability arising.

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