A COMPARATIVE ANALYSIS OF DIRECTORS' DUTIES OF CARE AND SKILL AND FIDUCIARY DUTIES OF LOYALTY AND GOOD FAITH UNDER THE COMPANIES' ACTS OF NIGERIA AND THE UNITED KINDGOM

By

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A THESIS SUBMITTED TO THE SCHOOL OF POSTGRADUATE STUDIES, AHMADU BELLO UNIVERSITY ZARIA, IN PARTIAL FULFUILMENT OF THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF MASTER OF LAWS (LL.M)

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DECLARATION

I declare that the work in this thesis entitled, A COMPARATIVE ANALYSIS OF DIRECTORS' DUTIES OF CARE AND SKILL AND FIDUCIARY DUTIES OF LOYALTY AND GOOD FAITH UNDER THE COMPANIES' ACTS OF NIGERIA AND THE UNITED KINGDOM, has been carried out by me in the Department of Commercial Law. The information derived from the literature has been duly acknowledged in the text and a list of references provided. No part of this thesis was previously presented for another degree or diploma at this or any other institution.

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Name of student	Signature	Date

CERTIFICATION

This thesis entitledA COMPARATIVE ANALYSIS OF DIRECTORS' DUTIES OF CARE AND SKILL AND FIDUCIARY DUTIES OF LOYALTY AND GOOD FAITH UNDER THE COMPANIES' ACTS OF NIGERIA AND THE UNITED KINGDOM by Hannatu ADAMU meets the regulations governing the award of the degree of Master of Laws of the Ahmadu Bello University, and is approved for its contribution to knowledge and literary presentation.

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ABBREVIATIONS

C.A.	Court of Appeal
CA	Companies Act
CAC	Corporate Affairs Commission
CAMA	Companies and Allied Matters Act
CBN	Central Bank of Nigeria
CEO	Chief Executive Officer
CH	Companies House
Ch.	Chancery
CLRSG	Company Law Review Steering Group
CSR	Corporate Social Responsibility
DBERR	Department of Business, Enterprise and Regulatory Reform
DTI	Department of Trade and Industry
EFCC	Economic and Financial Crimes Commission
ESV	Enlightened Shareholder Value
FWLR	Federal Weekly Law Report
J.C.A	Justice of the Court of Appeal
J.S.C	Justice of the Supreme Court
MP	Member of Parliament
MR	Master of the Rolls
No.	Number
NWLR	Nigeria Weekly Law Report
OECD	Organization for Economic Cooperation and Development
OFT	Office of Fair Trading
Pt.	Part
s.	Section
SEC	Securities and Exchange Commission
SPN	Shareholder Primacy Norm
ss.	Sections
SVM	Shareholder Value Maximization
UK	United Kingdom
US	United States
USA	United States of America
vs.	Versus

ABSTRACT

Having been in existence for about twenty five years now, the Companies and Allied Matters Act 1990 "CAMA" is long overdue for review. The many calls for the review of the law have not particularly singled out the director's duties of care and skill and fiduciary duties of loyalty and good faith. Yet, a cursory look at the statement of duties under the CAMA leaves much to be desired. The United Kingdom relatively recently reviewed its company law and now operates the Companies Act of 2006 "CA". One of the most admirable aspects of this new law is the codification of the duties of directors, which were hitherto uncodified and based in case law. For the fact that Nigeria is a common law jurisdiction which usually models its laws after English law, it will most likely be the case that any review of the CAMA today would have the CA as a foremost reference point. On this note, this research considered, comparatively, whether and to what extent the CA can be a model for the CAMA in the area of directors' general duties of care and skill and fiduciary duties of loyalty and good faith. A doctrinal method of research was employed using the tool of comparison. The research tried to show that the CAMA, after over 20 years, is far from being a model company law for Nigeria today in the area of the director's duties of care and skill and fiduciary duties of loyalty and good faith and therefore, requires review in line with the UK Companies Act 2006. The research found that the CAMA, although improved on the common law at the time of its enactment with respect to the standard of care required of the director, is far from being up to standards of today's business society. Furthermore, the fiduciary duties under the CAMA were found to be riddled with grammatical errors and in some cases, did not adequately reflect the common law principles they were meant to codify. The principles on conflicts of duties also gave the director very little information. Comparatively, the CA was found to be clearer on the points indicated and also reflected the modern practice on the standard of care required of directors. The work recommended that, on the duties of care and skill and fiduciary duties of loyalty and good faith, the CAMA should be amended substantially using the CA as a model. This would not only reflect developments from case law and practice, help to further clarify and simplify this important aspect of corporate governance for corporate stakeholders, but may also revive corporate litigation which is currently almost non-existent in that area.

CHAPTER ONE

GENERAL INTRODUCTION

1.1 Background

Companies have become an inextricable part of world economies. This is mainly due to the more prevalent capitalist ethos, but also because of the ease of investment and maximization of returns. Thus, beginning with the English Companies Acts of 1844-62, the state has constantly sought to regulate the corporation from creation, through to management and dissolution. The intention is not only to ensure that investment is easy, but also that it is as much as possible secure.

Though corporations are artificial persons, their directors, subscribers and customers, usually are not. Since human behaviour is prone to change in conformity with prevailing circumstances, opportunities, laws and more importantly, society, there exists a constant need to review and update corporate legislations to conform tothese changes. Sometimes, a review—which usually substantially overhauls the previous system—is what is required, but at times, a simple restatement, which maintains the old system in a new language, would achieve the desired goal in an amendment.

The first truly indigenous Nigerian companies' legislation was enacted in 1968. Before this, various corporate ordinances were promulgated by the colonial administration, from the Companies Ordinance of 1912 to the Companies (Amendment) Ordinance of 1954, later designated the Companies Act in 1963. Presently, the Companies and Allied Matters Act 1990 "CAMA" is in force.[1]Nigeria being a Commonwealth jurisdiction, has this company law anchored in English law; substantially an adoption of the English common law and equitable principles and

[1]Cap C20, Laws of the Federation of Nigeria, 2004. It was originally enacted by decree in 1990.

legislation on companies. Britain has a new UK Companies Act 2006 "CA".[2] The new law was a review of the UK Companies Act of 1985 which has so far been amended many times.[3]

Calls have been made from several quarters for the review of the CAMA.[4] It has been described as "stagnant and unprogressive".[5] That the many fines imposed by the law will not qualify as deterrent today, is hardly arguable. It is being suggested that the present law on companies is outdated and unworkable in today's business world which is fast becoming a global village. Public institutions, civil society organizations and scholars have expressed dissatisfaction with various aspects of the law.[6]For instance, Akume[7] has noted the need for a review in the areas of the investigatory and supervisory functions of the Corporate Affairs Commission (CAC), authorised share capital, guarantee companies, registration of business names and incorporated trustees. Adamu[8] on the other hand, has observed the need for extensive review in the area of the requirements for incorporation, in order to encourage registration and boost the Nigerian economy. The director-general of the Securities and Exchange Commission has expressed the hope that a reviewed CAMA would address the issue of women

[2] It was enforced piecemeal fashion from 2006 to 2009 when full implementation was achieved.

[3]In the years 1985, 1989, 1994, 1995, 1999, 2001. Aside this, there are a number of statutory laws that have been enacted from time to time to complement various provisions of the Companies Act.

[4] See for example Egwuatu, P. (2012, July 3).IFC Africa Calls for Review of CAMA.*Vanguard*. Retrieved August 21, 2012, from www.vanguardngr.com/; Egwuatu, P. (2012). PROSAN Moves for Amendment of CAMA.*Vanguard.*Retrieved April 26, 2014, fromhttp://www.vanguardngr.com/2012/10/prosan-moves-for-amendment-of-cama/; Eboh, M. (2009, September 24). Dematerialisation: Stockbrokers Call for Review of CAMA. *Vanguard*. Retrieved December 12, 2013, from http://www.vanguardngr.com/2009/09/dematerialisation-stockbrokers-call-for-review-of-cama/?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed%3A%20vanguardngr%2Fdleb%20%28Vanguard%20News%20Feed%29;Ekwere, U. (2010, November 1).Former SEC DG Calls for Amendment of CAMA.*Punch*.Retrieved December 6, 2013, fromwww.allianzeglobal.com/Market_News/.../AG_Market_News_011110_02.doc.

[5]Aina, K. (2013). Board of Directors and Corporate Governance in Nigeria.*International Journal of Business and Finance Management Research,* 1: 21-34, at p.23.

[6]See footnote 4 above.

[7]Akume, A. A. (2012). The CAMA 1990, 20 Years On: The Need for Some Review. *ABU Journal of Commercial Law*. 5(1): 28-39.

[8]Adamu, H. (2014). Towards Easing the Incorporation Process for Economic Transformation.*ABU Journal of Commercial Law*. 6(1): 205-219.

participation on the board of companies.[9] In his address to the public in the preface to the Companies Regulation 2012, the Registrar of the CAC revealed the Commission's hope of pursuing a comprehensive review of CAMA to address challenges faced that can only be resolved by amending the substantive law. In spite of these calls for review, however, the recent review of the CAMA only aimed at altering the mode of appointment of the chairman of the CAC and providing for the office of the secretary to the CAC and nothing more.[10]

Companies are undoubtedly important to modern economies. Therefore, directors who manage them are constantly in the limelight. In order to ensure security of investments, and discourage the abuse of the corporate machinery, certain principles have been developed over time to hold directors to certain obligations. This is because, while managing the company, directors wield enormous powers and control large funds generated mostly from the investing public. Thus, these legal principles, whether developed by the courts or introduced by legislation over time, have constantly sought to make directors more committed to, and accountable for, their offices in order to maintain certain standards. Some of such principles incorporated within legislation have acquired the status of *duty*.

'Duty' refers to an obligation; something that somebody is obliged to do for moral, legal or religious reasons.[11] In law, 'duty' is described as "a legal obligation that is owed or due to another and that needs to be satisfied; an obligation for which somebody else has a corresponding right.[12] Therefore, duties are usually couched in the tone of obligation, using any of the modal verbs 'shall,' 'must,' 'shall not' or 'must not.'

[9]Ogwu, M.S. (2014, April 18). We Encourage Quoted Firms to Have More Women Directors. *Daily Trust.*Business, p.22.
[10] See draft copy of the bill just passed at http://www.nassnig.org/nass/legislation_2012.php.
[11]Encarta Dictionaries (2009).Microsoft Encarta Premium DVD.
[12]Garner, A.B. (ed.). (2004).*Black's Law Dictionary.*8th edition, West Publishing Co., United States, p. 543.

However, 'shall' is generally considered old-fashioned today, when used to indicate obligation.[13] Nowadays, 'must' is preferred to emphatically indicate duty.[14]

Generally, the duties of directors are broadly categorized into two main heads: duties of *care* and *skill* and fiduciary duties of *loyalty* and *goodfaith.* In particular, the duties of care and skill are an aspect of the common law tort of negligence while the fiduciary duties sprung from equity.[15] All are adaptations of the expectation of the offices of trustee and agent, which a director often invariably is. The provisions in the two legislations under review have, using different styles, largely attempted to codify those common law and equitable connotations of the director's duties.

Of all the calls for the review of the CAMA, none has been aimed at the crucial area of the duties of directors. Scholars writing on the topic often do no more than restate the duties as provided in the Act. The scarcity of judicial decisions further suggests either inadequacy or ambiguity in that area. Many companies rather resort to removal of erring directors[16] or other such measures, than litigation, in resolving corporate governance issues. More scandalous cases are taken up by government agencies, such as the Securities and Exchange Commission, the Central Bank of Nigeria, or the Economic and Financial Crimes Commission, often reputed to be mere political tools of the prevailing political administration. In the light of the above, the question whether and to what extent the statement of directors' duties should also be reviewed—or at least, restated—in the light of new legislation and court decisions available for reference within the Commonwealth, is appropriate for discussion.

[13] See Encarta Dictionaries (2009). Microsoft Encarta Premium DVD, on the use of 'shall'.
[14] See Longman Dictionary of Contemporary English. (2005).4th edition, Pearson Education Limited, England, pp. 972-973.
[15]Wild, C. and Weinstein, S. (2009).*Smith & Keenan's Company Law.*14th edition, Pearson Education Limited, England, p. 334.
[16]As was the case in *Longe vs. First Bank of Nigeria Plc*. (2006) 3 NWLR (pt. 967) 228; (2010) All FWLR 258.

A cursory look at the CAMA in the area of directors' duties suggests that there is substantial need for restatement, and in some cases, review. S.279(1) begins with a contradiction in human nature, requiring directors to observe good faith not only during transactions on behalf of the company, but also during transactions with the company. S.279(2) purports to make directors agents of shareholders, even though only the company can enforce that fiduciary duty. S.279(3) proposes corporate objectives for every company and further confuses the standards by which the director's business judgment may be evaluated.

By far the most controversial of the statement of the duties, is s.279(4), which,in the same tone, requires the director to consider the interests of employees and members,without any apparent enforcement levers for the former group. Although s.279(5) acknowledges that a director shall exercise powers, it is not immediately apparent what those powers are or their likely source, so that the wording of the provision needs reconsideration. S.279(6) does not recognise any restrictions to the exercise of the director's voting power, which position would hardly be suitable for business today.

S.280 appears to be a poor result of the attempt to codify the common law principle against use of corporate property, opportunity and information, while s.287 appears to restrict prohibition of secret benefits to cases with the motive of inducement. Finally, in the case of the duty of care and skill, s.282 states the standard to be objective for all directors. Evidence from foreign jurisdictions increasingly shows this to be inadequate.

The latest review of the UK Companies Act is particularly notable for its codification of the duties of directors. Hitherto, these were simply anchored in common law and principles of equity standardized by case law. The policy makers entrusted with

the review—the Company Law Review Steering Group (CLRSG)—aimed to clarify and simplify the area for the average director in the hope of eventually improving corporate governance and also restating the corporate objective.[17]

The CA has now redefined the standard of skill and care required of the company director. Formerly under the earlier common law, the director's conduct was measured by purely subjective standardsand many court decisions in the late nineteenth and early twentieth century continuously endorsed this notion. Following criticisms from many quarters, however, the court eventually gave in and began to demand more from the director. Court decisions in the early 90's reflected that the company director was to be subjected to both subjective and objective standards. It is this modern view that is now reflected in s.174 of the CA.

On the various fiduciary duties, the CA has clarified the law and also made considerable changes. On the duty to act within powers conferred, the Act notes the company's constitution as the source of such powers. Importantly, the constitution includes any special resolution of members, not necessarily provisions of the articles. On the duty to exercise independent judgment, the Act recognizes that the director would not be in breach of the rule where he acts in accordance with any restrictive agreement entered into by the company or where his actions are sanctioned by the company's constitution. This is another area where the new law codified developments in case-law.

The general principles against conflict of interests involving exploitation of corporate property, corporate profiteering and self dealing, have been separated into three main heads of duties for clarity. S.175 deals with situational conflicts applying to exploitation of corporate property, information or opportunity. Although the CA, in

[17]See generally the Department of Trade and Industry's publication, *Companies Act 2006: Duties of Company Directors.*Retrieved April 26, 2014, from http://www.berr.gov.uk/files/file40139.pdf.

contrast to the common law here, allows authorisation of the conflict to be given by the board of directors, such an authorising board is required to be a disinterested one. On the duty against accepting benefits, the concept of reasonability is applicable in determining breach, just as it is in the duty above. Also, an associated company or persons acting on its behalf as well as the director's nominator, clearly do not constitute "third party" from whom the director must not accept benefits. As for transactional conflicts, declaration is required to be made to the other directors although nothing is mentioned of the authorising authority. Importantly, instances where such a declaration would not be required, have been made clear.

By far the most notable aspect of the codified duties in the CA, is s.172, which has generated the most debate, making it the most controversial. Here, the Act recognizes that although the foremost fiduciary duty of the director is to act in good faith to promote the success of the company for the benefit of the company's members as a whole, the director is required to consider other interests in achieving that aim. Hence, the interests of the company's employees, customers, suppliers, other business partners, host community as well as the environment, are factors which the director *must* consider. Furthermore, in the case of large or public companies, a business review is required to be tabled by the directors in their report, in which will be stated how far, if at all, any of the factors mentioned have been considered and, if not, the reason(s) why.

In arriving at this provision, the CLRSG had considered both the pluralist approach, characterised by giving equal status to all the company's stakeholders and shareholder primacy approach, which is a strategy that considers only the interests of the shareholders.In making their recommendations for the new companies law before its enactment, the CLRSG saw the overall objective of codifying the directors duties as one of achieving a "shareholder oriented, but inclusively framed, duty of loyalty", which

involved the recognition that, whilst the objective was to act in the collective best interests of shareholders, this could only be achieved by taking due account of wider interests.[18] The intention was to find a solution to the prevalent short-termism in the management of companies, by which management more often concentrated on simply making profits and declaring dividends, which attitude often resulted in unfavourable results for the company's stakeholders, particularly the members, in the long run. It was considered that an enlightened shareholder value approach would better achieve wealth and prosperity for all. This view recognizes that

> *directors will be more likely to achieve long term sustainable success for the benefit of their shareholders if their companies pay attention to a wider range of matters…Directors will be required to promote the success of the company in the collective best interest of the shareholders, but in doing so they will have to have regard to a wider range of factors, including the interests of employees and the environment*[19]

The duty in s.172 has been severely debated. While some have lauded it as improvement in the law,[20] others have found fault with the provision in varying degrees.[21] Unhelpfully, the provision has not been in force long enough for the courts to

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[18] *Developing the Framework,* a report of the Company Law Review Steering Group (CLRSG), published March, 2000, paragraph 2.22. It can be accessed at http://www.berr.gov.uk/bbf/co-act-2006/clr-review/page25086.html.

[19] Alistair Darling. Hansard. Commons Second Reading, June 6, 2006, column 125.

[20] See Arden, D.B.E. (2007). Companies' Act 2006 (UK): A New Approach to Directors' Duties. *Australia Law Journal,*81: 162-179; Clark, G.L. and Knight, E.R., (2008)*Implications of the UK Companies Act 2006 for Institutional Investors and the Market for Corporate Social Responsibility*.University of Pennsylvania Journal of Business Law. 11(2): 259-296. Retrieved April 22, 2014 from https://www.law.upenn.edu/journals/jbl/articles/volume11/issue2/ClarkKnight11U.Pa.J.Bus.L.259(2009).pdf;Hollington R. (2008, April 22).*Directors' Duties under the Companies Act 2006: Have the Lunatics Taken Over the Asylum?* A lecture delivered at Ian Fairbairn Lecture Theatre, University of Buckingham. Retrieved March 23 2013 from http://www.newsquarechambers.co.uk/files/Publications; Keay, A. (2007). Tackling the Issue of the Corporate Objective: An Analysis of the United Kingdom's Enlightened Shareholder Value Approach.*Sydney Law Review.* 29: 577-612, at 577.

[21] Woodley, J. (2011).Company Law Module Guide.*University of Hertfordshire School of Law*.2010/11, pp.62-63. Retrieved March 26, 2013, from http://www.scribd.com/doc/99319274/6LAW0087-Company-Law-2010-2011-Module-Guide; Davies, L.P. and Worthington, S. (2012).*Gower and Davies: Principles of Modern Company Law,* 9th edition, Sweet and Maxwell, London; Birds, J., et al. (2011).*Boyle and Birds' Company Law.*8th edition, Jordan Publishing Limited, Bristol.

provide any meaningful direction on the impact it may have. Yet already, many doubt that it would change the attitude of directors towards management or for that matter, the courts.[22]

During the review of the Nigerian Companies Act 1968, the English Companies Act of 1985 was one of the laws considered by the Nigerian Law Reform Commission, at the time. The informed expectation is that, should the Commission be saddled with a similar responsibility today, the present English Companies Act, which is relatively new, would be one of its foremost reference points. Therefore, comparative studies of the two laws would seem to be in order. The expectation is that the UK Act has taken into consideration certain developments which the CAMA, by virtue of the epoch of its enactment, could not have contemplated.

Due to the common origin of the two laws, similarities have been observed common to both legislations. For example, the director is still held to his good faith obligations when he acts on behalf of the company and his business judgment is still evaluated by subjective standards. However, where the director is required to consider the interests of a number of factors under the CA, he is required to consider the interests of primarily the company's employees and members under the CAMA. Whether or not this translates to any difference in practice, is debatable. Notably, the standard of care and skill required under the CA is markedly different from that under the CAMA. In the former, the director is judged by both objective and subjective standards, taking into consideration the job he performs and the experience and qualifications that he has. Under the CAMA, on the other hand, a uniform objective standard is applied.

Whether or not the duties as codified under the CA constitute the better legislation, is arguable. However, the fact remains that CLRSG's objective of clarity

[22] See Birds, J. et al., op.cit. at p.638 and Davies, L.P. and Worthington, S.op.cit. at p.543.

and simplicity has undoubtedly been achieved. In this work, the extent of review/restatement required under the CAMA as well as the extent to which the CA can be a model on that point, is considered.

1.2 Statement of the Problem

The CAMA has been in force some twenty-five years now. The many calls for its review have not addressed the area of directors' duties. Many of the scholars writing on this aspect of the legislation were more explanatory than critical of the provisions. Yet, a cursory look at the provisions on directors' duties in the CAMA suggested a need for review. Added to this is the scarcity of domestic case-law in this area. The new UK Companies Act 2006 had for the first time codified the duties of directors, breaking new grounds and standardizing developments from case-law. The question is, comparatively, whether and to what extent the UK Companies Act 2006 can be a model for the CAMA in the area of directors' general duties of care and skill and fiduciary duties of loyalty and good faith.

1.3 Aim and Objective

The research aimed to clarify the statement of directors' duties under the CAMA as well as bring them up to date with modern trends.Theresearch objective was to comparedirectors' general duties of care and skill and fiduciary duties of loyalty and good faith as codified under the CAMA and the CA, in order to show that the CAMA, after over 20 years, was far from being a model company law for Nigeria today and therefore, required review in line with the CA.

1.4 Scope of the Research

The research area was confined to the general duties of care and skill and the various manifestations of the fiduciary duties of loyalty and good faith as codified under the CA and the CAMA. The law was stated as at January 1, 2015.

1.5 Methodology

The research was doctrinal. The tool of comparison was used. The main legislations in the two jurisdictions, namely the English CA and the Nigerian CAMA, and case law, werethe primary sources for this work. The secondary sources included text books, theses, scholarly journals as well as newspapers, consulted appropriately. Internet sources featured considerably regarding the UK aspect of the work, being a foreign jurisdiction.

1.6 Literature Review

Nigerian authors addressed directors' duties in the light of the statutory provisions currently in force without more. Much of the literature considered in this area, were more explanatory than critical. Importantly, none of the writers set out with an objective as the one in this work: to compare directors' duties under the CAMA with those under some other jurisdiction.

Ogbuanya understoods.279(2) as imposing fiduciary duties on the director in favour of shareholders and any persons dealing with the company's securities.[23] Apparently, it did not occur to the author that the provision could be controversial especially considering s.279(9) allows the duty to be enforceable only by the company, to whom the director in fact owes his duties. Ali,[24] on the other hand noted the confusion suggested by the tenor of s.279(2) and suggested that the entire subsection is unnecessary due to the further statement in s.279(9) that the duty is enforceable only by the company.[25] These and more obvious flaws in the provision are observed further in this work.

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[23]Ogbuanya, N.C.S. (2010).*Essentials of Corporate Law Practice in Nigeria.*Novena Publishers Ltd., Lagos, at p.336.

[24]Ali, H.L. (1996).*The Powers of Directors in Nigerian Company Law: An Analysis of the Dynamic of Directors Dominance in Modern Companies.*(Unpublished LL.M. thesis).Faculty of Law, Ahmadu Bello University Zaria.

[25]Ibid. at p.168.

Regarding s.279(3), Emiola observed that the best interest of the company according to the subsection, is the faithful, diligent preservation of its assets to further its business and promote the purposes for which it was formed.[26] The fact will be debated in this work that companies, having been created for different purposes, may find their objectives changing with circumstances, so that corporate law cannot propose to set corporate objectives for them.

After observing that the duty to act in the best interests of the company is a subjective one, Bhadmus further noted that from the concluding part of s.279(3), the court would require some reasonableness, in the sense that the belief of the director must lead him to act in the manner of an ordinarily skilful director.[27] It is obvious that the author did not find anything untoward with the statement of the law here. This perception is challenged further in this work.

By far the one aspect of the fiduciary duties considered most controversial was the requirement in s.279(4) that the director regard the interests of employees in his duties. Emiola noted that the interests of the company's employees in general as well as the interests of its members were now assimilated into the best interests of the company, by virtue of s.279(4).[28] Ali on the other hand remarked that, though the provision bode well for employees and other stakeholders of the company, it was unfortunate that it was enforceable only at the company's discretion by virtue ofs.279(9).[29]Bhadmus also observed how the law neither provided the employees with means of enforcing the duty therein, nor even attempted to resolve the position where the interests of the members conflicts with those of the employees.[30]Ogbuanya simply considereds.279(4) a "mere

[26]Emiola, A. (2008). *Nigerian Company Law.*2nd editon, Emiola Publishers Limited, Ogbomosho, p. 396
[27]Bhadmus, Y.H. (2009).*Bhadmus on Corporate Law Practice.*Chenglo Limited, Enugu, pp.192-193.
[28]Emiola, A. op.cit.at p.397.
[29]Ali, H.L. op.cit.at p.185.
[30]Bhadmus, Y.H. op.cit.p.193.

pious declaration," as the right to enforce observance was not available for employees.[31] These criticisms suggest that a further analysis of the issue in this work is necessary.

Ogbuanya described the duties against conflicts of interest and secret benefits as the most challenging of directors duties.[32] On the duty of disclosure with respect to transactions with the company, he suggested that since the fine of N100.00 stipulated was ridiculous today, the general meeting may use a director's non-disclosure as grounds to remove him.[33]

As for the duty of care and skill, Orojo[34] suggested that the statement of the law in s.282 was as summarized by Romer J. in **Re City Equitable Fire Insurance Co. Ltd**.[35] This work will show why the learned author is mistaken here, with due respect. As rightly observed by Ogbuanya, the CAMA improved significantly from that common law position, so that the position in s. 282 is that the scale for judging the director's standard of conduct is objective, whereas this was subjective under the then common law.[36] The author believed that the imposition of such standards on the director by s. 282 thereby introduced professionalism to the office and was in line with the enormous powers vested in the company director under s. 63(3).[37] This work will show that there is room for improvement on the standard of care, considering developments from jurisdictions outside Nigeria.

Interestingly, it did not appear to have occurred to any of the aforementioned authors that the very first statement of the duties, i.e. s.279(1) was contradictory. Nor that many of the statement of the duties require disambiguation. All the authors mostly

[31]Ogbuanya, N.C.S. op.cit.atp.337.
[32] Ibid. at p. 340
[33]Ibid. at p.339.
[34]Orojo, J.O. (2008).*Company Law and Practice in Nigeria.*5th edition, LexisNexis Butterworths, Durban, South Africa, at p.269.
[35](1925) Ch. 425. See Ibid.
[36]Ogbuany, N.C.S. op.cit.at p.345.
[37] Ibid.

cited foreign decisions in explaining the principles of directors' duties and none of them noted this interesting fact of the scarcity of local decisions on the point.On the whole, it can also be concluded that,except in the few instances stated, they have not been overly critical of the CAMA in the area of discussion.

As for the CA, from ss.170-177[38] in the chapter appropriately titled "general duties of directors", a company directoris charged, under particular heads, with the duties to act within powers; promote the success of the company; exercise independent judgment, reasonable care, skill and diligence; avoid conflicts of interest; not to accept benefits from third parties; and to declare interests in proposed transactions or arrangements. For the first time, the duties which directors owe in England are clearly stated in unambiguous terms. Before now, much was left to the courts to decide on a case by case basis, based on principles of common law and equity.[39] Birds et al observed that it seemed clear from s.170(4) CA that the large body of case law that had established the duties in equity and at common law, would continue to be highly relevant, as would new case-law exploring the duties of fiduciaries in general.[40] As for the core duties of proper purpose and good faith, under ss.171 and 172 CA, the same authors were of the view that they appeared to do little more than set out the pre-existing law. This notion has been challenged by some optimists of the codified duties, particularly of s.172, as noted later in this work.

By far the most controversial aspect of the codified duties, was the provision in s.172,[41] which required directors to act in good faith in a manner most likely to promote

[38] See AppendixA attached.
[39] Hollington R. (2008).*Directors' Duties under the Companies Act 2006: Have the Lunatics Taken Over the Asylum?* A lecture delivered at Ian Fairbairn Lecture Theatre, University of Buckingham, April 22, 2008.Retrieved March 23 2013 from http://www.newsquarechambers.co.uk/files/Publications/Directors%20duties%20under%20the%20Companies%20Act%202006%20(Robin%20Hollington%20QC).pdf.
[40] Birds, et al, op.cit., p.630.
[41] See Appendix A.

the success of the company for the benefit of its members as a whole, while having regard to a number of listed factors. Woodley[42] expressed the suspicion that the provision may have been an attempt atintroducing stakeholder theory by the backdoor. Birds et al[43]and Davies and Worthington[44] were of the view that s.172 changed nothing from the previous law which required the director to, inter alia, consider the interests of employees.[45] They believed that in spite of the provision, directors would continue to reach the same decisions and the courts would continue to view these the same way. This may very well be the case.[46] However, Wild and Weinstein observed that the duty was beyond good faith, so that the six factors must find their way into every decision a director makes.[47] Thus, the factors to be considered are subservient only to the duty of directors to promote the success of the company.[48]

Sealy and Worthington[49] remarked that s.172 CA explicitly favoured a long-term, rather than short term, outlook in corporate decision making. Indeed, as observed further in this work, this was the effect the CLRSG intended the provision to have in theory. Whether or not it could potentially influence practice, is a different issue. Hollington argued that s.172 proposed to teach the business man how he should make business decisions[50] by venturing to state what the director must think,[51] whenthis should be the proper role of voluntary codes and business schools.[52] Arden, on the other hand, considered the section likely to improve the quality of corporate decision-making

[42]Woodley, J.op.cit., pp.62-63.
[43]Birds, J. et al.op.cit at p.638.
[44]Davies, L.P. and Worthington, S.Op.cit. at p.543.
[45] See s.309 UK Companies Act 1985.
[46] See Taylor, P. (2010). *Enlightened Shareholder Value and the Companies Act 2006.*(Unpublished doctoral dissertation).Birbeck College, University of London, England, p. 162. Retrieved May 24, 2014, from http://www.lccge.bbk.ac.uk/publications-and-resources/docs/PhDThesisPNTaylorJune2010.pdf.
[47]Wild, C. and Weinstein, S.op.cit., at p.331-332.
[48]Ibid., at p.332.
[49] Sealy, L. and Worthington, S. (2010). *Sealy's Cases and Materials in Company Law*.9th edition, Oxford University Press, New York, p.320.
[50] See Hollington R.Op.cit. at pp. 4 and 7.
[51]Ibid. at p.1.
[52]Ibid. at p.7.

with benefits for the rest of society, in addition to leading to a much greater consciousness on the part of companies of the debt they owed to the other groups which contributed to their success, in particular employees and the communities in which they operated.[53]Clark and Knight[54]also commended the provisions in s.172 at least in terms of giving legitimate voice to social and environmental issues and its ability to positively affect corporate social and environmental responsibility. The various differing views regarding this foremost fiduciary duty of directors clearly require closer consideration further in this work.

Regarding conflicts of interests, Hudson[55] opined that the principal effect of the statutory code was to provide directors with clear instructions as to how they could avoid their duties, so that under s.175, for example, directors could give one another authorization to take profits from their fiduciary duties. This, the author considered as having the potential to reduce the strictness of the fiduciary duty.[56] As observed further in this work, this may not have been the intendment of Parliament, as the latter simply wanted to introduce and simplify authorization in order to remove the taint of prohibition. Importantly, the requirement for a disinterested board to give the authorization, is expected to improve transparency in corporate governance.

On the duties of care, skill and diligence, Arden commended the fact that s.174 CAreflected the law as developed by the courts over time, as it took account of the special background, qualifications and management responsibilities of a particular director, while not excusing a director who lacked the basic attributes that a director

[53] Arden, D.B.E. Op.cit. at 173.
[54]Clark, G.L. and Knight, E.R. op.cit., at p. 295.
[55]Hudson, A. (2009). *Equity & Trusts.*6th edition, Routledge-Cavendish, section 12.5. Cited in Hudson, A. *Directors' Duties*. Being an early draft of a part of the author's contribution to Girvin, S., Hudson, A. and Frisby, S. (2010). Charlesworth's Company Law, 18th edition, Sweet and Maxwell.Retrieved December 26, 2013, from http://www.alastairhudson.com/companylaw/07%20-%20Directors%20duties%20-%20early%20web%20draft.pdf.
[56]Ibid. at p.7.

ought to have.[57] As noted later in this work, this view is increasingly becoming the modern trend, in spite of the fact that the company director is not required to have any particular qualification.

It is pertinent to note that none of the literatureconsidered even remotely attempted the task undertaken in this work, i.e. comparing the provisions on directors' duties in the two legislations under consideration. Thus, as far as is known, this work may very probably be the first of its kind.

1.7 Justification

This research is justified by the concerns raised in the Statement of the Problem. The law on companies in Nigeria, the CAMA, is long overdue for reform. A comparison of this law with the CA, would provide an idea of the direction and extent of review necessary in the area of directors' general duties of care and skill and fiduciary duties of loyalty and good faith. It is hoped that this would eventually be of immense benefit to investors, policy makers, other researchers and students. Most importantly, directors would gain enormously from a simpler re-statement of their duties, whose interpretationscurrently have to be extricated from a large corpus of case-law, most of which are from foreign jurisdictions.

1.8 Organizational Layout

This work is divided into six chapterswith each chapter concentrating, in the main, on a particular aspect of the work. Chapter One introduces the topic of the research. It starts by setting the background for the thesis. Here, the origins of the legislations under review are considered. But more importantly, this chapter singles out the research problem; outlines the scope; sets out the aims and objectives; analyzes literature on the point; reveals the methodology; and attempts to justify the research. Chapter Two

[57] Arden, D.B.E. op.cit at p. 169.

examines the concept of ‘director’ and his place within the corporate organization. Here, the meaning of “director” in relation to the company, is analysed. Further, the qualification, modes of appointment, status and the different types of directors, are respectively considered. The division of powers between the board of directors and the general meeting, both under the CAMA and the CA, is also discussed.

Chapter Three considers the duties of care and skill as well as the fiduciary duties which directors owe under the CAMA, just as Chapter Four analyses the same under the CA. Chapter Five weighs the similarities and dissimilarities between the two jurisdictions, while deciding the better law. The research is concluded in Chapter Six, with a summary of the findings and recommendations.

CHAPTER TWO

DIRECTORS UNDER NIGERIAN AND UK COMPANY LAWS

2.1 Introduction

Companies are the reason the office of company director exists. The word "company" or "corporation" has no strictly legal meaning.[1] But the entity often referred to as "company" in business circles, is a creature of law. A company can therefore be defined as that entity created by law through a process of registration, having the status and powers stated therein. Therefore, for an organization to be known as a company in that light, it must conform to the law creating it. Both the Companies and Allied Matters Act 1990[2] (CAMA) and the UK Companies Act 2006 (CA) create companies by registration,[3] and for purposes of either profit or charity. This work is mainly concerned with the companies created under the two laws above, viz. limited liability companies set up for business and charitable companies or companies limited by guarantee, which all require company directors.[4]

In the case of a sole proprietorship, the sole proprietor personally takes charge of the affairs of his venture. In fact, *he*is his venture. However, for the registered company, having a distinct personality and often, many shareholders, it becomes necessary to put a few persons in charge of matters for the whole. These few at the helm of affairs are the *directors*. In order for the capitalists (shareholders) to get returns for their investments and government to protect the public from fraud, company legislations have created certain principles regarding the person and office of the company director.

[1] Per Buckley J. in Re Stanley (1906) 1 Ch. 131 at 134.
[2] Cap C20, Laws of the Federation of Nigeria 2004.
[3] See ss. 35-37 CAMA and ss. 1, 7, 9 and 14-16 CA, respectively.
[4] See s.246 CAMA and s.155 CA.

The Nigerian Court of Appeal, in **Ladejobi vs. Odutola Holdings Ltd.**[5] identified the limited liability company as "a mere legal fiction that exists only in the eyes of the law."[6]Devoid of a functional brain and limbs, the artificiality of the person of the company necessitates the office of director within the entity. Lord Denning, M.R. observed as much, in the case of **Bolton (Engineering) Co. Ltd. vs. Graham & Sons,**[7]where he stated that "directors…represent the directing mind and will of the company, and control what it does...." Directors, in that sense, become the *brain* and *limbs* of the company. This grants every holder of the title enormous powers.

The Nigerian Supreme Court noted in the case of **Longe vs. First Bank of Nigeria PLC**,[8] that the employment of a director is one with statutory flavour, whereby "the employment is protected by statute." Consequently, the office is of great importance to the law in the organization of the corporation. Thus, the decisions as to who qualifies to occupy the office, how he gets appointed, the powers he may wield as well as the extent to which he may wield them, is regulated by law to a certain extent.

2.2 Meaning of Director

Ss. 244 of the CAMAand 154 of the CA require that any company established shall have directors.[9] It is therefore pertinent to discover the meaning of the term as used in relation to companies.

The term *director* is etymologically derived from the verb *to direct*, generally meaning to manage, instruct, order, orchestrate, control, supervise, oversee or even rule.[10] In relation to companies, the director is usually a natural person[11] entrusted with

[5](2002) 3 NWLR (Pt.753) 121 C.A.
[6]Ibid. at p.153.
[7](1957) 1 Q.B. 159.
[8](2010) All FWLR 258 at 307, paras.D-F.
[9] In the case of the CAMA, at least two for all types of companies and in the case of the CA, a minimum of one for private, and two for public, companies.
[10] See generally Encarta Dictionaries (2009).Microsoft Encarta Premium DVD and Longman Dictionary of Contemporary English.4th edition, Pearson Education Limited, England (2005), pp.439-440.

the power to make policy decisions together with his peers within that organization, in order to chart the course for the company. He is considered the alter ego (or other self) of the company by being the mind and brain behind its activities.[12]

It has been opined that the question *who is a director* may appear simple but is in fact often confusing.[13] This is perhaps because very few, if any, company legislations proffer the exact meaning of the term.[14] S.244 of the CAMA provides that directors "are persons duly appointed by the company to direct and manage the business of the company". The appointment here is presumably by the members of the company at the annual general meeting.[15] However, there are instances where persons, though not appointed by the company as such, are recognized as directors under the law. Such is the case with a shadow director, for example. In recognizing the latter, s.245 of the CAMA states that the term *director* "shall include any person on whose instructions and directions the directors are accustomed to act". In slightly different words, s.251 of the CA describes him as "a person in accordance with whose directions or instructions the directors of the company are accustomed to act". It is therefore clear that, apart from persons *duly appointed*, other persons not so appointed may fit the term.

Also negating the notion of due appointment is the fact that s.249(1) of the CAMA[16] empowers the board of directors to appoint a director to fill a casual vacancy which arises before the proper expiration of the tenure of one of their number. Any

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[11]Although theCA allows for corporate directors. See ss. 155, 164 and 251(3).
[12]Ogbuanya, N.C.S. (2010).*Essentials of Corporate Law Practice in Nigeria.*Novena Publishers Ltd., Lagos, p.324.
[13]Ibid., p. 323.
[14] This is true of the CA, for example. See Birds, J. et al. (2011).*Boyle and Birds' Company Law,* 8th edition, Jordan Publishing Limited, Bristol, p. 578.
[15] Refer to s.248 of the CAMA.
[16] As does s.168(3) of the CA.

person so appointed becomes a *director* to all intents and purposes for the duration of the period before the next annual general meeting.[17]

Again, even where a company does not officially appoint someone to the office of director, but holds him out as one or lets third parties assume he is that company's director, the law shall deem him as such for the purposes of any acts he may carry out for and on behalf of that company.[18] In such a situation, s.250 of the CAMA says that the company shall be bound by the acts of the person in question.

Upon careful scrutiny, it would seem that, in determining the question whether or not a certain person is a director, the law lays more emphasis on what a certain officer does, rather than his particular designation within the organization. In interpreting the term *director*, s.567 of the CAMA, like s.250 of the CA, says it includes "any person occupying the position of director, by whatever name called". This effectively makes irrelevant the exact name by which a person occupying the office is called, so long as he fits the description. In business climes today, there is a proliferation of titles by which holders of such an office are called within the organization. Titles such as president, CEO, manager, managing partner, governor, monitor, even trustee have, at some point, somehow found their way in corporate governance.

Jesse, M.R. in **Re Forest of Dean Coal Mining Co.**[19]likewise observed, regarding directors, that "…it does not matter what you call them, so long as you understand what their true position is, which is that they are really commercial men managing a trading concern for the benefit of themselves and of all other shareholders in it."[20]

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[17] See s.249(2) of the CAMA.
[18] Such a person may also be a director *by estoppel*, discussed under **2.5** infra.
[19](1878) 10 Ch. D., 450.
[20]Ibid., at 451-452.

The word *director* has not been defined by the courts to date. In considering the meaning of the term, the Nigerian Supreme Court,stated categorically that "the power to amend or vary the meaning of a director under CAMA has not been vested in a company concerned or the court."[21] The courts have therefore traditionally refrained from proposing any definitions of *director*, beyond the position stated in s.244 of the CAMA.[22]

Perhaps, this is as intended by the legislature, worldwide. The corporation has become a viable machine for sourcing capital. The fact that a lot of investment from the public goes into corporations, proves the imperative for regulation. In order for the law to be able to hold those persons accountable who carry out acts for and in the name of companies, it is wise that an exact definition of "director" is avoided and a description simply provided in the widest terms so that very few individuals would get away with using corporate organizations to perpetuate fraud or achieve other devious aims, in a way that the law would be unable to hold them accountable.

However, a working definition of the term should encompass both the duly appointed director as well as the one who acts as one. Thus, a director includes any person duly appointed to direct and manage the affairs of a company as well as any person occupying such a position in the company, whatever his official title, as well as any person on whose directions or instructions the directors of the company are accustomed to act.

2.3 Qualification for the Office of Director

[21] *Longe vs. First Bank of Nigeria Plc.Supra,* p.294.

[22] The Nigerian courts also in the cases of *Olufosoye vs. Fakorede* (1993) 1 NWLR pt. 272 at 747 and *Baffa vs. Odili*(2001) 15 NWLR (pt. 737) at p. 709, noted this position of the law.

The importance of the office of director necessitated legislation coming in to regulate its affairs within the organization. One aspect of such regulation is the law stating who cannot—and therefore, who can—be a company director.

S.257 of the CAMA provides that the following persons shall be disqualified from being directors:

a) An infant, that is, a person under the age of eighteen years;
b) A lunatic or person of unsound mind;
c) A person disqualified under ss. 253,[23] 254[24] and 258;[25]
d) A corporation other than its representative appointed to the board for a given term.

In addition, although a person who is seventy years or more may be appointed to the office of director of a public company, special notice is required for any resolution appointing or approving his appointment and notice must be given to the company and its members stating the fact of his age.[26]

Under the CA, the stance of the law is somewhat different. In the first place, s.157 of the Act sets the minimum age for appointment as director at sixteen. Previously common law accommodated someone as young as an infant for that post.[27] In fact, the law allows a person below the age of sixteen to be appointed, provided the appointment is not to take effect until such a person attains the required age of sixteen.[28] However, there is no maximum age for the appointment. Furthermore, the CA recognizes corporate directorship, so that there can be members of the board of directors who are not in fact natural persons but corporations. Nevertheless, all companies must have at least one director who is a natural person.[29]

[23] An insolvent.
[24] A fraud convict.
[25] A person required to vacate his office of director under the circumstances listed under that section.
[26] See s. 256 of the CAMA.
[27] See *Re Cardiff Savings Bank (Marquis of Bute's Case*), (1892), Ch. 100, where the Marquis was appointed to the office at the tender age of 6 months.
[28] Refer to s. 157(2) CA.
[29] Refer to s. 155 CA.

Also, the UK for some time now has had in force the Company Directors Disqualification Act 1986, which generally disqualifies certain persons in certain situations from being involved in the formation or management of companies and, in particular, from being company directors.[30] The Insolvency Act 2000 also later came to compliment the latter. The net effect of the two legislations is to disqualify persons based on issues ranging from conviction for offences, persistent default, fraud and unfitness, to wrongful and fraudulent trading and competition infringements, from appointment as company directors. This is done through the instrumentality of disqualification orders or undertakings. The period of disqualification may range from two to fifteen years,[31] but may be relaxed by the court which may give leave to the disqualified person to act in a particular case. Pursuant to this, the Secretary of State is required to maintain a register of such persons for the reference of the public. A similar arrangement is not applicable in Nigeria. It is submitted that the publication of the names of persons who are declared unfit to manage companies in future can help investors immensely when it comes to the choice of managers or enterprises.

It is pertinent to note that there are generally no formal qualifications for eligibility for appointment into the office of director under both company legislations:[32] neither examinations to write nor certificates to present.[33] Indeed, the courts have long established that "a director is not bound to bring any special qualification to his

[30] See s. 11 of the Company Directors Disqualification Act 1986.
[31] Refer to s.6 Company Directors Disqualification Act 1986.
[32] Although the articles can require share qualification.See s. 251(1) CAMA and s. 400(5) CA by implication.
[33] However, there are industry-specific legislations, such as the Banks and Other Financial Institutions Act "BOFIA", which require directors not to have prior criminal record of offences relating to fraud or dishonesty. In fact, in the case of banks, ss.19 and 44 BOFIA provide that a management agent, director or chief executive may not be appointed without the prior approval of the Central Bank of Nigeria. Corporate codes also generally encourage directors to be knowledgeable in business and financial matters. See for example s.5.3.2 of the Central Bank of Nigeria (CBN) Code of Corporate Governance Post Consolidation, 2006.

office."[34] A director is not even required to know his statutory duties. In spite of this, any occupier of that office is still held strictly to his obligation of discharging his duties within a reasonable standard of care, skill and diligence. It is submitted that at least for the duly appointed director, with reference to the statutory duties of care and skill and fiduciary duties of loyalty and good faith, a prospective director should be required to know and understand their purport, at the company's expense, before officially taking up his position in the company.

2.4 Appointment of Directors

The appointment of persons to the office of director within the company is largely an issue for the consideration of members, in the first instance, in order that investors may have some hold on the running of the company. The Nigerian Court of Appeal opined as much when it stated, in the case of **NIB Investment W/A vs. Omisore,**[35] that "…the appointment of directors is the business of the general meeting or the board of the company, and not that of any individual member."

However, the exigencies involved in the running of the company have seen the law allowing for appointment of persons to the office through the medium of 'outsiders', or even upon assumption of the law. This is all in order for company operations to go smoothly and accountability to be more certain.

Generally, in discussing their appointment, directors are necessarily categorized into *firstdirectors* and *subsequentdirectors*.

2.4.1 First Directors

Before the company takes off and begins business, in fact, while pre-incorporation details are being considered, it is necessary for the directors of the supposed entity to feature and play important roles in meeting the requirement of the law, especially

[34] Per Neville J. in *Re Brazillian Rubber Plantation Estate Ltd*. (1911) 1 Ch. 425
[35] (2006) 4 NWLR (pt. 969) 172 at p. 199.

regards signing important pre-incorporation documents, such as the corporate constitutional documents. These must be tendered to the appropriate government agency,[36] before the company would be granted certificate of incorporation permitting it to commence business.

Consequently, the first directors must necessarily be appointed even before the company comes into being. The few available avenues here are the incorporation documents, such as the memorandum and articles of association[37] and other prescribed statements to be tendered. S.247 of the CAMA provides that "the names of the first directors shall be determined in writing by the subscribers of the memorandum of association or a majority of them or the directors may be named in the articles." In different words, s.16(6)(a) of the CA says that "the persons named in the statement of proposed officers as director…are deemed to have been appointed to that office."

As part of the incorporation process, incorporators are required to file special documents specifically for details regarding the directors of the proposed company. In the case of the CAMA, s.35(2)(c) provides for the first directors by requiring "a statement in the prescribed form containing the list and particulars together with the consent of the persons who are to be the first directors of the company" to be delivered to the Corporate Affairs Commission (CAC) together with other documents of incorporation.[38] Likewise, s.12 of the CA requires a statement of the proposed officers, in particular, "the person who is, or persons who are, to be the first director or directors

[36] The Corporate Affairs Commission, in the case of Nigeria and the Companies House, in the case of the UK.

[37] S.41 of the CAMA considers that, once registered, these have the effect of a contract under seal between the company and its members and officers and between the members and officers themselves. Likewise, s.33 of the CA considers the company's articles as covenants between the company and each member.

[38] In practice, a Form CAC 7, obtained from the CAC, is simply filled and filed to meet the requirement of the law.

of the company" to be presented at the Companies House (CH) as part of the incorporation requirements.

The tenor of the different laws above implies that the mere act of the inclusion and identification of the names of any persons as *directors*, in either or all of these documents, formally seals their appointment to such an office. There is in fact no further need for the company to ratify their appointments when it eventually formally comes into being.

2.4.2 Subsequent Directors

Once the company is duly incorporated, it then becomes a person in law,[39] capable of, among other things, employing labour and entering into contracts in its own name. Consequently, it can also hire or appoint officers, including directors, in accordance with procedures laid down by law as well as the company's own constitution: the articles of association.

In most instances, except a few, the CA leaves the province of appointment of subsequent directors largely to the articles to prescribe. Depending on the circumstances, however, the following have power under the CAMA or the articles of association, to appoint directors for the company:

1. *The Annual General Meeting.* It is generally stated in s.248 of the CAMA that "the members at the annual general meeting shall have power to re-elect or reject directors and appoint new ones." The tenor of the law here implies that even the articles of association cannot deprive the members of this statutory power. Also, s.249(3) grants the general meeting the ultimate power of increasing or reducing the number of directors generally as well as determining in what rotation directors shall retire. This is in alignment with the general idea

[39] Refer to s.38(1) of the CAMA.

of granting the members of the company the means of charting the course for the company and checking the excesses of directors. The general meeting is attended by all who have a stake in the company by virtue of the share(s) they hold. The law considers that they have the most to gain or lose from the company being in capable or incapable hands. Therefore, more than any other persons, the members should decide who takes part in the running of the company.

2. *The Board of Directors.* Particularly after the occurrence of instances the law presumes as causing a "casual vacancy" in the office of a director in any company, s.249(1) empowers the board to appoint new directors to fill the vacuum so created. However, this power is limited by two points. Firstly, apparently, the vacancy must arise only from the death, resignation, retirement or removal of a serving director, and not from any other occurrence. Secondly, s.249(2) makes the appointment *subject to* the approval of the members at the very next annual general meeting. Otherwise, any director so appointed ceases to hold that office on the day of the said meeting. Also, by virtue of s.249(3), the board may increase the number of directors so long as that increase does not ultimately cause the number at any given time to be more than the maximum number of directors allowed by the articles. The CA also suggests that the board of directors may fill a casual vacancy in their number,[40] but only one arising out of the removal of a serving director.
3. *Any Person Specified by the Articles.* The law allows companies to confer powers on any named person—even an outsider—to appoint or remove a director of the company. According to s.41(3) CAMA, "where the

[40]Refer to s.168(3)

memorandum or articles empower any person to appoint or remove any director or other officer of the company, such power will be enforceable by the person notwithstanding that he is not a member or officer of the company." This practice is often employed by private companies where the majority shareholder wishes to hold on to the reins of the business or where an investor invests his money in a company using other people as a façade, only to try to control the business from 'outside' by causing the articles to appoint him as nominator of the company's directors. It has been opined based on a number of decisions, that if the appointer exercises his power of appointment, the company would be bound to accept and if it refuses, the appointer may enforce his power by injunction, though he is not likely to succeed if the appointee is unsuitable on personal grounds or if he merely had a right to nominate a candidate, and not to appoint a director.[41] It is also imperative to note and emphasize that the power so conferred on any particular person to appoint or remove directors, must be expressly contained in either of the two corporate constitutional documents—the memorandum or the articles.

4. *Personal Representatives.* Where all the members of the company die, the law permits "any of the personal representatives…to apply to the court for an order to convene a meeting of all the personal representatives of the shareholders entitled to attend and vote at a general meeting to appoint new directors to manage the company".[42] This is due to the exigency of the situation. The idea of the concept of the company envisages existence in perpetuity so that the death of one or all of the company's members or officers should not result in the end of that entity. Thus, at any point in time when all the members die at

[41]Orojo, J.O. (2008).*Company Law and Practice in Nigeria,* 5th edition, LexisNexis Butterworths, Durban, South Africa, p. 252.
[42]S.248(2) of the CAMA.

once and none has survived to convene a meeting to decide the direction for the company, personal representatives will automatically step in to take their place, pending the proper administration of the dead members' estate.

5. *The Creditors.* Where all the directors and members of the company are dead and their personal representatives, for one reason or the other, fail to convene a meeting to appoint new directors to manage the company, the law permits the creditors of the company, if there are any, to convene such a meeting and thereby appoint new directors for the company.[43]

Where there are no creditors as well or they also fail to convene a meeting, the law is silent. Such a situation is yet to be presented before the courts. Perhaps then, any *sufficientlyinterested party* may apply to the court for directions. Otherwise, the company effectively becomes defunct.

2.5 Types of Directors

From the nature of their appointment, the kind of services they render within the company and their tenure in office, the following types of directors have generally been recognized in many corporate literature:

i) *Executive and Non-Executive Directors*:- In corporate governance, which is a set of ideas essentially concerned with the proper management of companies for desired returns, there is often a two-tier board system in public companies whereby directors are often categorized into executive or full-time directors and non-executive or part-time directors, so that the former would see to managing the daily affairs of the company, while the latter would simply attend and lend their ideas at periodic meetings as the board for that company. The law says a director is simply someone

[43] Ibid.

appointed to "direct and manage the business of the company".[44] The Supreme Court observed, in **Longe vs. First Bank of Nig. Plc**,[45] that this definition of directors above does not recognize the nomenclature "executive/non-executive".[46] When the Court of Appeal in **Longe vs. First Bank of Nig. Plc.**[47] sought to differentiate executive from non executive directors on the basis of their directorial status, the Supreme Court decided eventually that "all directors, whether executive or non-executive, are the same as long as they are all engaged to direct and manage the business of the company."[48] However, in practice, some persons to be appointed to the office need not in fact be particularly skilled in the company's operations and may only be required to give policy advice or simply draw investors' confidence in the company simply by allowing their names to be associated with it. Most often, a company appoints directors with the required skills and know-how to see to the practical, day-to-day aspects of management. These are the *executive directors*. They may also be referred to as service directors owing to the fact that they are often also salaried managers or employees of the company under contracts of service. On the other hand, in order to garner goodwill and tap from experienced persons in the way of business strategy and policy formulation, the company might, in addition, also appoint persons who, though very busy men, are of great repute and can attend to certain needs of the company when consulted once in a while. These are the *non-executive directors*. More often, this classification of executive/non-executive is not found in corporate legislation but in corporate codes of

[44]See s.244(1) of the CAMA.
[45](2010) *Supra.*
[46]Per Oguntade, JSC., at p. 294.
[47](2003) 3 NWLR (pt. 967) 228.
[48] Per Oguntade JSC, (2010) All FWLR, at p. 296.

ethics. In fact the only two instances it is directly mentioned in the CAMA are in s.244(2) on presumption of due appointment and s.282(4), where the same standard of care is required for both executive and non executive directors with the possibility of a higher standard in the case of an executive director.Executive directors have added duties and responsibilities as employees and managers of the company working under specific contracts of employment.[49]

ii) *Independent Director*:- This is a non-executive director, also known in board circles as an "outsider", often placed on the board of a public company specifically to lend an independent and objective judgment to its activities. He is a creature of American corporate literature of the 70s. Corporate scandals gradually led to a review of the functions of the board from an advisory board characterized by consultation activities, to a monitoring board entrusted with both control and strategy guiding functions.[50] The independent director was to be the harbinger of this radical change in board functions. To achieve this, his description is often explicitly provided in corporate codes. For example, paragraph 5.5 of the Nigerian Securities and Exchange Commission (SEC) Code of Corporate Governance for Public Companies (2011) requires an independent director to be a person who is not a substantial shareholder, nor a supplier or customer of the company. He must not be a member of the immediate family of any person with strong ties to the company. Similarly, paragraph B.1.1. of the UK Corporate Governance Code (2012) suggests that he must not have been an employee

[49]Irukwu, O.J. (1994).*The Company, the Shareholder, the Director and the Law,* Fourth Dimension Publishing Co. Ltd. Enugu, p. 72.

[50]Pirani, P. (2013).*Independent Directors in Publicly Traded Companies: Origin and Evolution Over Time*. Retrieved May 26, 2013 fromhttp://papers.ssrn.com/sol3/papers.cfm?abstract_id=2261239&download=yes.

of the company within the last five years nor had any material business relationship with it within the last three years. He should not be a representative of a significant shareholder nor have any close family ties with any of the company's officers. The OECD Principles of Corporate Governance (2004) requires a sufficient number of such independent directors to form board membership and specifically carry out tasks where there is a potential of conflict of interest such as financial reporting, nomination of board members and deciding board remuneration. Though known in corporate codes of ethics worldwide, he is hardly mentioned in company legislations. The most important thing is that he must appear so independent of the board, that his views would be objective and unbiased enough to give the shareholders and prospective investors balanced information so that they in turn can make an informed judgment.

iii) *Alternate and Assignee Directors*:- The articles of a company may allow a duly appointed director to delegate his powers to another, who shall exercise the powers of the director appointing himfor a while. Such appointee becomes an *alternate*. Alternate directors are usually created for administrative convenience, especially where an alien is involved,[51] so that the alternate would usually be a local/resident director. Thus, delegation in this sense is usually the preserve of non-executive directors, who are not often on hand. The alternate also has the power to resign. Assignee directors, on the other hand, are appointed by sitting directors to hold brief for them for the long haul. In **Baffa vs. Odili,**[52]the court distinguished alternate from assignee directors by stating that alternates are appointed by directors, who

[51]Ogbuanya, N.C.S. op.cit., p. 326.
[52](2001) 15 NWLR, Pt. 737, at 709.

are allowed to temporarily delegate their functions under the articles of a company, while in the case of an assignee director, such delegation of powers and duties is of a more permanent nature.[53]

iv) *Managing Director:*-This is a title usually employed for the chief executive officer of the company: the head of *management*. The holder of this title takes full responsibility for the activities of the company and derives his powers from delegation by the board, in accordance with the articles of association. The law recognizes the office in question in that s.64(b) *permits* the board of directors to, from time to time, appoint one or more of their body to the office of managing director and delegate all or any of their powers to such managing director. S.263(5) further provides that, in the exercise of the powers so delegated to him, he shall conform to any regulations that may be made by the directors. He is therefore answerable to the board. It is important to note that a *managing director* is, prima facie, a *director* within the meaning of the law. The Supreme Court emphasized this fact in **Longe vs. First Bank of Nig. Plc**.,[54] when it stated that, "under any definition, a managing director is the directing mind and will and the *alter ego* of the company, through which the company acts."[55] Subject to the terms of any employment contract between him and the company, he shall also be entitled to remuneration determined by the directors.[56] The managing director is usually, though not necessarily, a member of the board of directors of the company, so that he holds dual positions both as alter ego

[53]Bhadmus, Y.H. (2009). *Bhadmus on Corporate Law Practice,*Chenglo Limited, Enugu, p. 177.
[54](2010) Supra.
[55]Per Oguntade, JSC, at p. 295.
[56] Refer to s.268(1) of the CAMA.

and employee of the company.[57] This implication can be drawn from the wordings of s.64(b) CAMA. He also ceases to hold office, if for any reason he ceases to hold office as a director.[58] Corporate codes of ethics available today suggest that the board should, as much as possible, be independent of management in order to play the role of overseer to check the excesses of executive directors.[59] Therefore, ideally, the managing director should not, at the same time, be the chairman of the board, although he may be a board member.[60] It is noteworthy that the CA neither mentions nor provides for the managing director, leaving it entirely to the articles to do so.

v) *Representative/Nominee Director:*-The CAMA prohibits corporate directorship, so that corporations by themselves and in their names, cannot occupy the office of director in any company.[61] However, a *representative* of a company can be nominated and then appointed to the board of another company for a given term. In the particulars of directors in the form of Form CAC7 filed by the company, such a director is reflected as a representative/nominee of the company that has appointed him.[62] Where the articles permit,[63] a particular shareholder or class of shareholders or even a creditor, may be empowered to nominate a director on the board. The latter becomes a *nominee* of the shareholder or creditor.

[57] Ogbuanya, N.C.S. op.cit., p. 325.
[58] See *Yalaju-Amaye vs. Associated Registered Engineering Contractors Ltd*. (1978) All NLR, 124.
[59] See for example ss. 2.2 and 4.5 of the Securities and Exchange Commission (SEC) Code of Corporate Governance for Public Companies in Nigeria, 2011 and s. 5.3 Central Bank of Nigeria (CBN) Code of Corporate Governance for Banks in Nigeria, Post Consolidation, 2006.
[60] The Organization for Economic Cooperation and Development (OECD) considers this good practice. Refer to paragraph E, page 65 of the OECD Principles of Corporate Governance 2004.
[61] Refer to s. 257(1)(d).
[62] Ogbuanya, N.C.S. op.cit., at p. 328.
[63] As suggested by s. 41(3) of the CAMA.

vi) *De Facto/De Jure Director:-* A *de facto* director is described as a person who has not been formally appointed and neither has the relevant government agency been notified of his appointment in the papers filed by the company, as would have been the case for a *de jure* director. Yet, he is a director "in fact". He is treated as a director by the courts if there is a dispute, because he has *acted* like a director and therefore, must take legal responsibility for those actions as if he was one. Thus, one would usually not hear about him unless there was some trouble. If *de jure* directors are persons *duly appointed* by the company to direct and manage the business of the company,[64] then it follows that *de facto* directors are persons who, though not duly appointed by the company, in fact direct and manage the business of the company. Their liability is such that, where they act on behalf of the company, their acts shall not bind the company and they shall be personally liable for such actions, unless it can be proved that the company held them out as its director.[65] In **Re Paycheck Services 3 Ltd**.,[66] the UK Supreme Court recently reviewed the meaning of de facto director in the case of a large number of companies that had the same single corporate director. The issue was whether the only active director of the latter could be regarded as a de facto director of the companies and held accountable for unlawful dividends paid by those companies. The decision of the Court of Appeal[67] was upheld that the mere fact that a director of a company acts on behalf of that company in its role as a corporate director of another company does not by itself make that individual a de facto director of the latter

[64] See s. 244(1) of the CAMA on "the meaning of directors."
[65] See s. 250 of the CAMA.
[66](2010) UKSC 51, (2011) 1 BCLC 141.
[67](2009) EWCA Civ 625, (2009) 2 BCLC 309.

company.[68] A de jure director, on the other hand, is a director "in law", i.e. whose appointment is recognized by the law and documented as such with the relevant government agency. He has the proper mandate of the company to act on its behalf. The company will take full responsibility for any actions he may take within that mandate.

vii) *Director by Estoppel:*-where a person not duly appointed to the post of director acts as one, without the company holding him out as its director, he is fully responsible for his actions and any liabilities he may incur. He becomes a "de facto director" by virtue of his actions. However, where a person, though not duly appointed a director of a company, is held out by the company as its director, then he thereby becomes a director of the company in his dealings with any third parties to whom such representation was made. The company then becomes liable to any such third party and becomes *estopped* from denying the fact of his directorship.[69] For example, the company may make such misrepresentation of him to the public through the particulars of directors it files with the companies registry.[70]

viii) *Life Director:*- S.255 of the CAMA states that a person may be appointed a director for life, although removable under the Act. This appointment may either be in the list of first directors presented to the CAC at incorporation or simply by appropriate designation in the articles.Such a director must vacate his office, should any of the situations listed in s.257, happen to him. However, he is neither subject toretirementnor rotation as is normally the case with other directors. In practice, he is more often a founder, co-founder or major shareholder in a private company and his tenure is acknowledged

[68] Birds, J. et al. *op.cit.*, p.579.
[69] See generally s. 250 of the CAMA.
[70] Refer to s. 69(b) of the CAMA.

by the articles. He often holds "preference" or "founders" shares, which are of a special class with special rights attached.

ix) *Shadow Directors:-* In order to identify those with real influence on corporate affairs other than professional advisers,[71] corporate law acknowledges the existence of the shadow director. He is described as "any person on whose instructions and directions the directors are accustomed to act."[72] In practice, identifying him is no easy task. In the first place, the law clarifies that persons who give advice in their professional capacity, upon which directors act, do not fall under this description.[73] This effectively excludes lawyers, auditors and other such professionals periodically engaged by the company for expert advice. It has been suggested that there is no need to show in all cases that the properly appointed directors cast themselves in a subservient role or surrender their respective discretions.[74]Nevertheless, the words "accustomed to act" in s.245 of the CAMA, require some *pattern* and a single instruction, however significant, will not suffice. In his dealings with the company, the shadow director is bound by the same rules of conduct as the company's directors, especially in those areas where conflicts of interest may arise.[75] However, the UK Court of Appeal in **Ultraframe (UK) Ltd. vs. Fielding**,[76] held that although a shadow director is subject to the requirements imposed by a number of statutory provisions, he does not normally owe fiduciary duties to the company. Perhaps this is because fiduciary duties arise from the fact of one party reposing trust on the other.

[71]Per Morritt L.J. in *Secretary of State for Trade and Industry vs. Deverell (2000) 2 B.C.L.C 133.*
[72] See s. 245(1) of the CAMA and 251(1) of the CA.
[73] Refer to s. 245(3) of the CAMA.
[74]Per Morritt L.J., in *Secretary of State for Trade and Industry vs. Deverell* supra.
[75]Irukwu, O.J. *op.cit.*, p. 73.
[76] (2005) EWHC 1638 (Ch)

Since the company can be said to be "officially unaware" of the shadow director, clearly it has not placed any trust on him.The judgments of Lords Collins and Walker of the UK Supreme Court in **Re Paycheck Services 3 Ltd**.[77] suggest that de facto and shadow directorships can overlap, where the facts indicate that someone is both a shadow director in respect of certain functions and a de facto in respect of others. In the latter case, he would be subject to the full range of fiduciary duties.[78] Judicial decisions in the UK, such as in **Re PFTZM Ltd.**[79]have expanded upon the definition of shadow director indicating that a corporate body can also be identified as one.

It is pertinent to note that S.244(2) of CAMA provides that there shall be every rebuttable presumption that all persons who are described by the company as directors whether as Executive or otherwise, have been duly appointed. Accordingly, whenever the appointment of a director is called to question, there is a presumption of validity regarding his prior acts, notwithstanding any defect that may afterwards be discovered in his appointment or qualification.[80] This is in order to protect third parties that might have transacted with him in good faith, without this knowledge.

2.6 Status of Directors

There are various ways through which a holder of the title of "director" may come to it: if the company does not outrightly appoint someone a director, the law may deem him so. But, however a director comes to his office, the law considers from the onset that he takes actions for and on behalf of his company, which is a person in law. In simple terms, therefore, he is a representative.

[77]Supra, at 91 and 110.
[78]Birds, J. et al. Op.cit., p. 581.
[79](1995) BCC 280.
[80] See ss. 260 of the CAMA and 161 of the CA.

Generally, a director is an *officer* in the company,[81] like any other official who holds any administrative post within the corporation. He may also be a mere *employee*, if he is employed by the company under some contract of service,[82] simply. This would most often be the case with the executive director, also known as *service director*. However, as observed by the Nigerian Supreme Court in **Longe vs. First Bank of Nig. Plc.**,[83] this still does not derogate from the fact of his *directorship*, as long as he is seen to be directing and managing the business of the company.

According to s.283(1)

> *Directors are trustees of the company's moneys, properties and their powers and as such, must account for all the moneys over which they exercise control and shall refund any moneys improperly paid away, and shall exercise their power honestly, in the interest of the company and all the shareholders, and not in their own or sectional interests.*

Further s.283(2) states that "a director may, when acting within his authority and the powers of the company, be regarded as agent of the company…." This much was emphasized by the court in **Trenco. Nig. Ltd. vs. African Real Estate and Investment Co. Ltd.,**[84] wherein was stated that a company, although having a corporate personality, is deemed to have human personality through its officers and agents, the directors being such.[85]

In the relationship between the company and other persons, and with respect to the functions he performs and any legitimate powers he may wield, a director is an agent in the general sense of the word.[86] This stems from the fact of the company being

[81] Refer to ss. 567 of the CAMA and 12 and 16(6) of the CA.
[82] Refer generally to ss. 291 of the CAMA and 188 and 227 of the CA.
[83](2010) Supra.
[84](1978) All NLR, 124; (1978) NSCC 220.
[85]Per Aniagolu J.S.C.
[86] Refer to s. 283(2) of the CAMA. See also the Supreme Court decision in *Yusufu vs. Kupper International* (1996) 5 NWLR (pt. 446) 17.

an artificial person which, by its nature, cannot act on its own. Based on this, a fiduciary duty is contemplated by the law on the part of the director, towards the company.[87] In fact, s. 279(1) states emphatically that a director stands in a fiduciary relationship towards the company. More to the point, in the course of deciding**Ferguson vs. Wilson**,[88] it was stated that

> *They (directors) are merely agents of the company. The company itself cannot act in its own person, it can only act through directors and the case is, as regards those directors, merely the ordinary case of principal and agent. Whenever an agent is liable, those directors would be liable, where the liability would attach to the principal and the principal only, the liability is the liability of the company.*

However, in the typical agency, the principal usually has a complete set of detailed instructions for his agent as to what he requires of him. Also, the agent can get feedbacks from the principal regarding any eventuality that may be encountered and how the principal wants the agent to go about handling it. Further, the agent cannot venture into uncertainties by taking risks. But this cannot be the case with the director of a corporation. He makes the policies, strategizes how to put them in action and goes ahead and puts them into practice. In doing so, he takes risks. In fact, it has been said that risk is the essence of a director's work.[89] To be sure, a director is a more powerful agent than most. The modern view is that his position within the corporation is essentially *sui generis.*[90]

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[87] See *Okeowo vs. Migliore* (1979) 11 SC, p. 113

[88](1866) LR.2 CH. 77.

[89]Olawoyin, G.A. (1977).*Status and Duties of Company Directors,* University of Ife Press, Ile-Ife, *p.7.*

[90] See Birds, J. *et al,* op.cit., p. 627; Campbell, C. (2007).*International Liability of Corporate Directors*.Volume 2,Yorkhill Law Publishing, London, p. 97; Cornelius, G., Van der Merwe. (2004).*Introduction to the Law of South Africa*, Kluwer Law International, Netherlands, p. 384; Dyson, B.R. (1965). The Director's Liability for Negligence. *Indiana Law Journal,* Indiana University, U.S.A.40(3): 341 at 346.

Owing to the enormous powers wielded by a director, the law also attributes to him the role of trustee with regard to the monies and properties of the company.[91] Yet, directors are not trustees properly so called.[92] Unlike the regular trustee, the company's properties would not be in his name and, as mentioned above, the trustee is expected to observe a higher standard of prudence in protecting the interests of his or her beneficiary than would be reasonable to impose on a person in charge of a commercial company.[93] A director is entitled to take risks with the company's monies, if he considers it likely to be in the best interests of the company. However, under no circumstances is he allowed to use his position to enrich himself, make secret profits or achieve other unnecessary benefits owing to the office he occupies.[94]

Whatever act of the directors is called to question, they are judged either as agents or trustees; quite simply, fiduciaries. Birds *et al*succinctly summed it up in stating that

> *The absence of a definition of 'director' perhaps renders it somewhat difficult to ascertain the exact nature of the director's office. He is certainly an agent of the company, but is rather more than that as in practice, he is not subject to much control by his principal, the company acting through the shareholders in general meeting. In certain respects, the director is a trustee and there is no doubt that many of his duties developed from the law of trusts, but he is certainly not a full trustee, not least because his very function is an entrepreneurial one and he may properly take risks with the company's funds which a trustee in the strict sense cannot. If a director performs more than the tasks of a director pure and simple, such as attending board meetings and the like, he may well also be an employee of the company and as such the*

[91] See s. 283(1) of the CAMA and

[92]*Adebayo vs. Johnson* (1969) All NLR, 171.

[93] Davies, J. (2007).*A Guide to Directors' Responsibilities Under the Companies Act 2006.*Certified Accountants Educational Trust.RetrievedMarch 27, 2013 from http://www.accaglobal.com/content/dam/acca/global/PDF-technical/business-law/tech-tp-cdd.pdf.

[94]See generally ss. 280 and 287 of the CAMA and 175-177 of the CA.

> *beneficiary of important statutory rights if he is declared redundant or unfairly dismissed. In short, the director's office is sui generis, although for certain purposes the analogies of agency, trusteeship and employment may be useful.*[95]

Indeed, as we shall observe later in this work, all the duties owed by directors, or functions required of them by law, can somehow be subsumed under the roles of trustee, agent or employee. It is often in one or more of these roles that the law seeks to hold them to account.

2.7 Division of Powers between the Directors and the General Meeting

It is clear that a company in and of itself cannot perform any acts: the law which recognizes the existence of the person of the corporation also recognizes the imperative of requiring it to have *organs* through which it may manifest the purpose of its existence. The members on the one hand and the directors on the other, between them control the powers of the company as its organs. The two legislations under consideration approach this issue in slightly different ways.

S.63(1) of the CAMA emphatically states that "a company shall act through its members in general meeting or its board of directors or through officers or agents, appointed by or under authority derived from the members in general meeting or the board of directors." Ideally, the members here, meaning the shareholders, appoint a board of directors, which in turn sets the business objectives and directions for the company, while the day-to-day operations are carried out by the management led by the chief executive officer. The board and management thereafter become accountable to the shareholders in the general meeting.[96]

S.63(2) follows to reveal that the aforesaid powers are to be determined by the articles, which is the *constitution* by which the company is governed. The provisions of

[95] Birds, J. et al. op.cit., p. 627.
[96] Ogbuanya, N.C.S. op.cit., p. 321.

the CAMA on this point will only apply where the articles of a company are silent. Thus, the Act has carefully refrained from setting power boundaries for the two organs. In fact, any articles may grant a particular board overriding powers over members and vice versa. The idea is that, as articles are alterable by resolution,[97] members would always have the chance to change the power ratio,[98] should they be displeased with the directors' report or general performance. They may also refuse to re-elect erring directors or even remove them, outrightly. Perhaps, for this reason, the law has made it "easy business" to remove a director, by requiring simply an ordinary resolution.[99] Furthermore, the board may exercise any power which has not been specifically reservedby the articles or CAMA for the general meeting.[100]

Although the CAMA recognizes the ideal role of the board of directors in the management or administration of the company, to the extent of granting it residual powers of the company,[101] it does not thereby grant the board a free rein over every affair of the company involving administration and management. In order to allow for a system of checks and balances in company management, s.63(5) allows the general meeting to:

a) Act in any matter if the members of the board of directors are disqualified or are unable to act because of a deadlock on the board or otherwise;
b) Institute legal proceedings in the name and on behalf of the company, if the board of directors refuse or neglect to do so;
c) Ratify or confirm any action taken by the board of directors; or
d) Make recommendations to the board of directors regarding action to be taken by the board.

This provision is effective whether or not provided for in the articles. That is to say, the articles cannot purport to deny the members in a general meeting these statutory

[97] Refer to s. 48 of the CAMA.
[98] But not to thereby invalidate the previous acts of the directors. Refer to s. 63(6) CAMA.
[99] Refer to s. 262 of the CAMA.
[100] Refer to s. 63(3) of the CAMA.
[101] Refer to s. 63(3) of the CAMA. It has been suggested that this flows from the doctrine of necessity. See Emiola, A. (2008).*Nigerian Company Law.*2nd edition, Emiola Publishers Ltd. Ogbomosho, p. 336.

rights.However, barring the four instances stated above or an alteration of the power ratio in the articles, the general meeting cannot direct the board to do or refrain from doing a particular act. From the above, therefore, the board's powers under the CAMA are derived from (a) the Act, (b) the articles and, (c) residual powers.

A third organ of the company is often recognized in the office of the managing director,[102] sometimes called the "chief executive officer" or CEO. Although the latter is an appointee of the board of directors, it is in him that the real executive powers of the company are vested in modern times.[103] The role of the CEO was further explained by the court in **Virgin Tech Ltd. vs. Mohammed & Bank PHB**.[104] In that case, the respondent, who was a director and co-signatory to the Appellant's bank account, caused the transfer of the sum of N199,660,000.00 (one hundred and ninety-nine million, six hundred and sixty thousand naira), from the latter's account to her personal account with the second respondent. When attempts at persuading her to return the money failed, the CEO then instituted an action in the name of the company against the respondents. The first respondent raised the issue whether the CEO had locus to do so. Ruling on the authority of the CEO to act on behalf of the company, the court, per Dongban-Mensen J.C.A. observed that

> *the CEO of a company has a responsibility to keep an eye on the possessions of the company. As the CEO, he maintains a supervisory role over the officers of the company. His authority to act on behalf of the company is accordingly implied.*[105]

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[102] Refer to s.64(b) of the CAMA. See Ikhariale, M.A. (1980).Democracy, Capitalism and the Corporate System: Another Look at the Rule in Foss vs. Harbottle.*A.B.U. Law Journal*, 4-8: 51 at 55, quoting Loss, L. (1980). *Trends in Corporate Governance and Investors Protection,* p. 51.

[103] Ali, H.L. (1996).*The Powers of Directors in Nigerian Company Law: An Analysis of the Dynamic of Directors Dominance in Modern Companies,* LL.M. thesis (unpublished) Faculty of Law, Ahmadu Bello University Zaria, p.77.

[104](2009) 11 NWLR (Pt.1151) 136 C.A.

[105]Ibid., at p.149, citing *Sotuminu vs. Ocean Steamship (Nig. Ltd.)*(1987) 4 NWLR (Pt.66) 691.

The court thus recognized this conduct of the CEO as coming within the contemplation of the combined effect of ss.63 and 65. Evidently, in spite of the fact that he is not directly mentioned in the CAMA, the law recognizes the CEO as a most senior officer in the company, capable of acting single-handedly on its behalf, when justified by the circumstances.

In the UK jurisdiction, the division of power between the general meeting and the board is based on slightly different principles. Unlike the CAMA, the CA has made no express provision in the usual manner, leaving the company's articles to determine it.[106] The model articles provided by the CA appear to allow the articles to substantially decide the power ratio as between the board and the general meeting.

Generally, the rule under common law used to be that where powers of management were vested in the directors, they alone could exercise these powers. The only way in which the general body of the shareholders could control the exercise of powers vested in the directors was by altering the articles, or, if opportunity arose under the articles, by refusing to re-elect the directors of whose actions they disapproved. They could not themselves usurp the powers which, by the articles, were vested in the directors any more than the directors could usurp the powers vested by the articles in the general body of shareholders.[107]The decision in **Automatic Self-Cleansing Filter Syndicate Co. Ltd vs. Cuninghame,**[108]held that where the general management of the company is vested in the directors, the members have no power by ordinary resolution, to give directions to the board or to overrule its business decisions. However, under the CA now, the combined effect of ss. 17, 29 and 257 is to allow the members to direct the board to take or refrain from taking a particular action, even in matters reserved for the

[106] Sealy, L and Worthington, S. (2008).*Cases and Materials in Company Law.*8th edition, Oxford University Press Inc., New York, p.175.
[107] Per Greer LJ, English Court of Appeal on *John Shaw and Sons (Salford) Ltd vs. Shaw* [1935] 2 KB113, cited in Sealy, L and Worthington, S. *op.cit.*, p.179.
[108](1906) 2 Ch. 34.

directors' powers by the articles.[109] Therefore, the company's reserve powers may be exercised by the general meeting by special resolution, without altering the articles. This is particularly ideal for urgent matters which cannot wait for the cumbersome process of altering the articles.

The English court has established as a general rule that the company in general meeting may act if there is no board competent or able—for example, because of a deadlock—to exercise the powers conferred upon it. It is believed that "there must be some power in the company to do itself that which, under the circumstances would be otherwise done."[110] This rule is not negated by the CA. Thus, if the articles do not provide for powers in the event of a deadlock, etc. the general meeting can generally act.

Conclusively, the board's powers here are derived mainly from (a) the Act, (b) the articles and (c) resolutions and agreements of the general meeting. It is pertinent to note that in taking their decisions, the board of directors is a collegiate body. Yet, as will be observed later in this work, the directors owe their duties personally.

The arrangement discussed above would more often be the case for public companies. In some private companies, where the members happen to be the directors as well, the powers of the company in practice would appear fused. In such cases, the board of directors and the general meeting would most certainly be represented by the same persons.

[109] See also the proposed model articles supported by the CA, which are applicable to companies by default. See in particular Article 4(1), Schedule 1 Regulation 2, UKModel Articles for Private Companies Limited by Shares and Article 4(1) Schedule 3 Regulation 4, UK Model Articles for Public Companies, effective from April 28, 2013.

[110] *Barron vs. Potter* (1914) 1 Ch. 895. See also *Foster vs. Foster* (1916) 1 Ch 532.

CHAPTER THREE

DUTIES OF CARE AND SKILL AND FIDUCIARY DUTIES OF LOYALTY AND GOOD FAITH UNDER THE COMPANIES AND ALLIED MATTERS ACT

3.1 Introduction

The duties company directors owe under the Companies and Allied Matters Act 1990[1] "CAMA" are anchored in English law, specifically principles of common law and equity.[2] As the Nigerian corporate legal system is fairly young,[3] there are relatively few local decisions supporting the provisions in the CAMA. Indeed, Nigerian courts more often rely on English decisions to arrive at their own conclusions. In order to have a thorough discussion in this chapter therefore, considerable dependence on English authorities cannot be avoided.

Directors being essentially trustees and agents, the duties they owe are mainly categorised into two: those relating to *care and skill* and then*loyalty and good faith.* Accordingly, the following discussions are generally grouped under corresponding headings. Any reference to "director" shall allude to both the *de facto* and *de jure.* With respect to shadow directors particularly owing duties to the company, the CAMA is silent. Under common law, a shadow director does not normally owe fiduciary duties.[4]However, more recent judicial authority suggests that he may owe the duty to act in good faith towards the company, at least in relation to the directions or instructions he gives the others.[5]Any reference to sections or "the Act" herein shall be to the

[1] Cap C20, Laws of the Federation of Nigeria 2004.

[2]In particular, the duties of care and skill are an aspect of the tort of negligence while the fiduciary duties sprung from equity. See Wild, C. and Weinstein, S. (2009).*Smith & Keenan's Company Law.*14th edition, Pearson Education Limited, England, p. 334.

[3] With the first indigenous companies law promulgated by decree in 1968, i.e. the Companies Decree No. 51 of 1968. Prior to this, there were various ordinances periodically made by colonial administrators.

[4]*Ultraframe (UK) Ltd. vs. Fielding* (2005) EWHC 1638 (Ch).

[5] See ***Vivendi SA vs. Richards* (2013) EWHC 3006.**

CAMA, unless otherwise stated. For clarity, "company", "firm" and "corporation" will be used interchangeably as having the same contextual meaning.

3.2 General Duties of Directors

Directors being persons in charge of the management of the company, their duties to the company are inarguably non-exhaustive. This fact springs from the idea of their being the "minds and limbs of the corporation". This therefore means that they are constantly called upon to perform one action or the other in the name of the company. Thus, while they are required to go about their job displaying reasonable care and skill and also uphold their loyalty and good faith to the business, they are also obligated, given the relevant circumstances, to appoint the secretary,[6] prepare and present the financial statement,[7] make the declaration of solvency,[8] initiate suits in the name, and on behalf, of the company,[9]and give certain notices to the company.[10] While every duty of the director is important, this research is limited to the all-pervading general duties of care and skill and fiduciary duties of loyalty and good faith, discussed in broad terms, and expected of each director, personally.

3.3 Duties of Care and Skill

These duties have a common law base. A prominent feature of the limited company which had a bearing on the development of the duties of care and skill was that the concept of limited liability ensures that the members of a company are able to limit their personal liability to the company's creditors for the company's debts. Thus, both shareholders and creditors have always had to accept significant financial risks in their

[6] Refer to ss. 295 and 296.
[7] Refer to ss. 334 and 345.
[8] Refer to s. 462.
[9] By implication, s. 63(3) and (5)(b).
[10] See ss. 276 and 277, for example.

dealings with company directors. The duties of care and skill evolved as a means of restricting those risks to an acceptable level.[11]

The duties border on the manner in which a director is required to act in discharging his obligations. As noted earlier in this work,[12] the law does not demand of directors to hold any special skills or qualifications in order to be appointed to office. However, it has been held that since the directors control what the company does, the conferment of such powers on them entitles shareholders and stakeholders of the company to the best of services.[13]

In simple terms, "care" means attention shown in order to avoid damage or error.[14] "Skill" refers to know-how; an ability to do something well, especially because one has learned and practised it.[15]A third though less prominent aspect of the duty, is "diligence" which connotes "working hard" while being "careful and thorough."[16] It is also considered to be a term which equates to conscientiousness and attentiveness.[17] Apparently, "diligence" carries a meaning similar to a combination of "care" and "skill" and is used for emphasis. This may explain the reason why some commentators and even judges neglect it altogether in interpretation. In relation to directors' duties, all three are more often called "the duty of care and skill" as in the CAMA or simply "the duty of care," although *care*, *skill* and *diligence* may each have its notional meaning.[18]
In imposing the duties of care and skill upon the director, the law raises the question of the standard of care to be expected as well as the level of personal attention required of

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[11] Davies, J. (2007).*A Guide to Directors' Responsibilities Under the Companies Act 2006.*Certified Accountants Educational Trust, England, p. 31.Retrieved March 27, 2013, from http://www.accaglobal.com/content/dam/acca/global/PDF-technical/business-law/tech-tp-cdd.pdf.
[12] Please, refer to **2.3** above.
[13] See *Delta Steel Nigeria Ltd. vs. American Computer Tech Inc.* (1999) 4 NWLR pt. 597
[14]Encarta Dictionaries (2009).Microsoft Encarta Premium DVD.
[15]Longman Dictionary of Contemporary English.(2005).4th edition, Pearson Education Limited, England, p. 1547.
[16]Ibid. at 436.
[17]Davies, J.op.cit., p. 38.
[18]Corkery, F.J. (1987).*Directors' Powers and Duties*. Longman Cheshire, Melbourne Australia, p. 131.

him. Romer J. deliberated on these points while deciding the English case of **Re City Equitable Fire Insurance Co.**,[19]which decision was considered the authority on the point for a long time, at common law. In that case, the chairman of an insurance company committed frauds by purporting to buy treasury bonds just before the end of the accounting period and selling them just after the audit. By this method, a debt due to the company from a firm in which the chairman had an interest was considerably reduced on the balance sheet by increasing the gilt-edged securities shown as assets and the auditors could not detect this. It appeared that the directors of the company had left the management of its affairs almost entirely to the chairman and it was perhaps because of this that he had more easily been able to perpetuate his frauds.

After some very careful deliberations, Romer J. reached the following conclusion:[20]

> *i) A director need not exhibit in the performance of his duties, a greater degree of skill than may reasonably be **expected from a person of his knowledge and experience**. A director of a life insurance company, for instance, does not guarantee that he has the skill of an actuary or of a physician. In the words of Lindley M.R., if directors act within their powers, if they act with such care as is reasonably to be expected from them, having regard to their knowledge and experience, and if they act honestly for the benefit of the company they represent, they discharge both their equitable as well as their legal duty to the company. It is perhaps only another way of stating the same proposition to say that directors are not liable for mere errors of judgment.*
>
> *ii) A director is not bound to give continuous attention to the affairs of his company. His duties are of an intermittent nature to be performed at periodical board meetings and at any meetings of any committee of the board upon which he happens to be placed. He ishowever, **not bound to attend all such meetings** though he ought to attend whenever, in the circumstances, he is reasonably able to do so.*

[19](1925) Ch. 407.
[20]Ibid., at p. 428.

iii) *In respect of duties that, having regard to the exigencies of business, and the articles of association, may probably be left to some other official, a director is, in the absence of grounds for suspicion, justified in trusting that official to perform such duties honestly. (emphasis added)*

Romer's decision above substantially agrees with a much earlier position held by Bacon VC in**ReMontrotierAsphalte Co (Perry's case)**:[21]

> *It is not part of the duty of a director to take part in every transaction which is conducted at a board meeting. His business or his pleasure may take him elsewhere and it would be a most unheard of thing to say that if anything wrong was done at a board meeting, he being named among the directors but not present, he is liable for what is done in his absence*.[22]

Many other decisions on the same point reached in cases reported in the late nineteenth and early twentieth centuries also took similar positions. In **Re Cardiff Savings Bank (Marquis of Bute's Case)**,[23]for example, the English court had held a director not liable for certain irregularities in the lending operations of a bank, despite having attended a company meeting only once in 38 years.[24]Apparently, he was only appointed to lend the company the prestige that came with his family's title and no more. In the words of Jessel MR, "neglect or omission to attend meetings is not the same thing as neglect or omission of a duty which ought to be performed at those meetings."[25]Thus, it is better to stay away from meetings than to attend and be inattentive.[26]Following this, the court also decided, in the case of **Re Brazilian Rubber Plantation and**

[21](1876) 34 LT 716.
[22]Ibid., at 717.
[23](1892) Ch. 100.
[24] A similar decision was reached in the case of *Re Denham* (1883) 25 Ch. D. 752, where a director attended no meetings in a four-year period and therefore, was held not liable regarding a fraud that had occurred.
[25] Supra, at p. 109.
[26]Corkery, F.J. op.cit., p. 136. Consider also the dictum of Lord Hatherley in *Land Credit Co. of Ireland vs. Fermony* (1870) LR 5 Ch. App. 763 at 770-771, that "it is their (directors') duty to be awake (during meetings) and their being asleep would not exempt them from the consequences of not attending to the business of the company."

Estates,[27]that a director may undertake the management of a rubber company in complete ignorance of everything connected with rubber, without accruing responsibility for the mistakes which may result from such ignorance, for "he is not bound to bring any special qualifications to his office."[28]

The common law propositions above clearly set more of a subjective, than objective, standard for the director in discharging his duties. In effect, the courts were saying that "the director is obliged only to do as much as could be expected from someone as incompetent and foolish as he happens to be."[29]It has been opined that the courts' summations may have had non-executive, rather than executive, directors in mind, possibly because of the then popular belief that the non-executive director had no serious role to play within the company but was simply "a piece of window-dressing aimed at promoting the company's image."[30] It has also been suggested that Parliament and the courts did not want to discourage entrepreneurial activity by restricting access to the company format. Further, given the wide range of backgrounds from which directors could legitimately come, it would have been unrealistic to expect the conduct of all directors to be judged by a single benchmark.[31] In any case, several scholars have since criticized the laxity in standards proposed by the decisions, particularly the fact of their being unsuitable for modern time[32]and being unduly generous to the incompetent

[27](1911) 1 Ch. 425.
[28]Per Neville, J. ibid.
[29] Mackenzie. (1982). A Company Director's Obligations of Care and Skill.*Journal of Business Law,* 460 at p. 461. Cited in Finch, V. (1992).Company Directors: Who Cares About Skill and Care?*The Modern Law Review*, 55(2): 179-214, at p. 200.
[30] Davies, L.P. and Worthington, S. (2012).*Gower & Davies: Principles of Modern Company Law.*9th edition, Sweet and Maxwell, London, p. 518.
[31]Corkery, F.J. op.cit., p. 142 and Davies, J. op.cit., pp.39-40.
[32] See Ogbuanya, N.C.S. (2010).*Essentials of Corporate Law Practice in Nigeria.*Novena Publishers Ltd., Lagos, p. 345; Olakanmi, O. & Co. (2006).*Companies and Allied Matters Act: Synoptic Guide*.Lawlords Publications, Abuja, p. 41; Ali, H.L. (1996).*The Powers of Directors in Nigerian Company Law: An Analysis of the Dynamic of Directors Dominance in Modern Companies.*LL.M. thesis (unpublished) Faculty of Law, Ahmadu Bello University Zaria, p. 155; Mbah, D.E. (1987).*A Comparative Study of the Nigerian Companies' Act 1968 and the Ghana Companies Code 1963*.LL.M. thesis (unpublished) Faculty of Law, Ahmadu Bello University Zaria, pp. 101-102; Gower, L.C.B. (1961).*Final Report of the Commission of*

director.[33]In calling for higher standards, Gower argued, "as the business world comes to expect higher standards, the law should develop in step. What has handicapped legal development so far has been the failure of the courts to recognise that 'directing is becoming a profession with developing standards of expertise."[34] Thus, having minimal or no knowledge in connection with the line of business of a particular company can no longer be tolerated of directors.

Apparently inspired by the plethora of condemnation and in a bid to set the record straight and improve upon the standard hitherto set by the English cases, the drafters of the CAMA at the time came up with the following provision in s. 279(3): "a director shall act at all times...in such manner as a faithful, diligent, careful and ordinarily skilful director would act in the circumstances." More to the point, s. 282(1), provides that "every director of a company shall...exercise that degree of care, diligence and skill which a reasonably prudent director would exercise in comparable circumstances." It is not clear from the Act what "prudent" and "diligent" mean. The dictionary meaning of "prudent" has connotations of "care" or "being careful".[35] As earlier observed, though "diligence" was part of the duty at common law, it was not the most prominent part of it. Whenever it is mentioned, it is usually simply lumped together with "care and skill." From all indications, it is more probably seen as an extension of the duty of care.

In order to further emphasise the duty in subsection (1), subsection (2) warns that "failure to take reasonable care in accordance with the provisions of s.282 of this Act shall ground an action for negligence and breach of duty."To ensure that the

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Enquiry on the Company Law of Ghana, p. 146; Worthington, S. (2001).*Reforming Directors Duties*. London School of Economics (LSE) Research Online, pp.9-10. Retrieved March 24, 2013, from http://eprints.lse.ac.uk/archive/00000200.

[33]Finch, V. op.cit. note 28 at p.179

[34] Gower, L.C.B. (1961). In: *The Report of the Commission of Enquiry on the Company Law of Ghana*.

[35]Encarta Dictionaries (2009).Microsoft Encarta Premium DVD.

director gives adequate care and attention to his duty to the company, and in order to deliberately deviate from the English court's ruling in **Re City Equitable Fire Insurance Co.**above, Section 282(3) provides that "each director shall be individually responsible for the actions of the board in which he participated, and the absence from the board's deliberation, unless justified, shall not relieve a director of such responsibility."

Evidently, contrary to the position held by Orojo,[36] the position in Nigeria today is not the same as the common law at the time of the ruling by Romer J. The drafters of the CAMA deviated from the common law position noted by deliberately setting clear, objective standards in the sections mentioned above, perhaps due to the obvious inadequacies observed in the subjective standard.

Essentially, the CAMA differs from the propositions proffered in the English cases in three ways. Firstly, by requiring the director to measure up to the standard of any "reasonably prudent director", the law thereby subjects him to an objective, reasonable man test. Thus, if a company appoints a moron, it is well within its rights to still expect him to measure up to the standard of a notional, reasonable director. It has been suggested[37] that the standard now seems to be set somewhere "between the level of the ignoramus or moron at one extreme and that of a top flight professional director at the other extreme." The provision therefore has the potential of encouraging any prospective director to decline a position he knows he is incompetent to fill.

Conversely, this also implies that, should any particular director in fact possess more skills or qualification than reasonably to be expected of the reasonable man or average director in his circumstance, he would still only be held accountable by the

[36]Orojo, J.O. (2008). *Company Law and Practice in Nigeria.*5th edition, LexisNexis Butterworths, Durban, South Africa, p.269.
[37]Osunbor, O.A. (1992).*The Company Director: His Appointment, Powers and Duties.* In: Akanki, E.O. (ed)Essays on Company Law, p. 130, at 147.

reasonable man's standard and the company cannot expect more from him, unless his service contract states otherwise. This may have the undesirable effect of not encouraging directors to acquire further skills or qualification or even neglecting to put them to use, where they possess them. Although s. 282(4) leaves no doubt that the same standard of care is required of both executive and non executive directors, a proviso further allows any service contract with the company to demand a higher standard or place additional liability in the case of the executive or service director.

Secondly, by providing that each director shall be *individually responsible* for the actions of the board in which he participated and, in the event he was absent, can be exonerated only when such absence can be justified, s. 282(3) thereby demands of the director to give considerable attention to attending meetings and, when he does attend, to consciously advert his mind and pay special attention to proceedings, in order to guard against liability. This effectively makes non-executives who may not even attend board meetings, responsible for any act or omission that may have occurred in their absence, if they cannot justify their absence from the meeting. Obviously, the law here does not consider the director's duty as being of "an intermittent nature" or one which requires him to attend meetings only when convenient. Thus, were the **Marquis of Bute's Case** to be tried under the CAMA today, the Marquis would likely be found liable in negligence or breach of duty[38] having attended a company meeting only once in 38 years.

Thirdly, by cautioning the director against delegating his powers in a manner that may amount to an *abdication of duty*, s. 279(7) thereby encourages the director to be mindful of his obligations to the company, even where he delegates another to do the work. Granted, requiring the director to display reasonable care and skill implies that he

[38] Refer to s. 282(2) CAMA.

himself is involved in the act of discharging his duty. Yet, it is conceded that due to some circumstantial exigency and the nature of the services directors provide for the company, it may be necessary for directors to delegate some tasks or responsibilities to other persons and indeed, the terms of their appointment may allow them to do so. On the other hand, the law realises the need to curtail unrestrained or excessive delegation of duties on the part of directors in order to curtail the abuse of the discretion given.

Exactly the extent of delegation likely to result in an "abdication of duty" is not clear. However, since the section does permit delegation *primafacie*, it is likely that "abdication of duty" may be alluding to the issue of supervision. Therefore, a director is allowed to delegate, but he must not only ensure that the delegated responsibility is discharged in the proper manner and with the required standard of skill and care, but must also only delegate such tasks as do not, by their nature, require his own personal attention or expertise. Presumably, if he must delegate, then he should ensure to delegate to someone competent.

The case of **Adebayo vs. Johnson**,[39] though a misfeasance proceedings decided under s. 211 of the Companies Decree 1968, is here presented as a classic example of a case of a company destroyed by the incompetence and carelessness of its directors. In that case, the Merchants Bank Ltd. had incurred a lot of losses and was being liquidated. Prior to that, at a meeting of the board of directors held on 29th July 1959, the managing director had reported that about £30,000 was unaccounted for in the books of the bank. Although the minutes of that meeting showed that the manager was directed to prepare and submit to the board a statement of the financial position of the Bank as at the 31st July, 1959, the minutes of several subsequent board meetings showed that no mention was made of the matter again nor did any of the directors express any concern about the

[39](1969) All NLR, 171.

loss of this amount of about £30,000 or any expectation that the situation should be righted. Meanwhile, the losses of the bank steadily soared to about £63,000 in September, 1960. Coker J.S.C. found that it was particularly appalling on the part of the directors that none of them, except the managing director, took any steps to see that the manager complied with their directives, if only to request an investigation of the report by a firm of auditors. Coker J.S.C. then set the record straight on the issue of delegation, observing that

> *A director of a company is not expected to fill all the positions in the company himself and he should be entitled to assume that qualified staff are performing the duties of their offices with competence. He is certainly not expected to abdicate his responsibility but he is undoubtedly entitled to rely on the judgments of responsible assistants with the requisite knowledge, training and expertise. We do not think that any inherent distinction lies in the duties and liabilities of categories of directors; but the Chairman of the Board of Directors and the Managing Director may by the Articles of Association of the company, and must by the nature of their special access and connection with the detailed machinery of control, be expected to know better than the other directors.*[40]

On the matter of the liability of the directors under the circumstances, the Supreme Court had no difficulty holding them liable for deficiency after they were put on notice of irregularities, yet still did nothing.

> *If one looks again at the authorities on the subject and examines the conduct of the directors, it is impossible in our view to resist the inference that with respect at least to the amount representing the increase in the losses of the Bank from some £37,000 in July, 1959 to some £63,000 in September, 1960, they were guilty of such conduct as is tantamount to gross negligence of their responsibility and we do not entertain any doubt that the loss of this amount of £26,506.17s. 10d. was due entirely to this condition. In the events that have happened, they*

[40] Ibid., at 187.

> *must pay over this amount into the assets of the company and they will be jointly and severally liable to do so.*[41]

Though the decision above was decided based on the Companies Decree of 1968, the principle observed is no different from that in the present Act. Although the court admitted the director's right to delegate as was observed in **Re City**, yet the court was quick to caution that he must not thereby *abdicate* his responsibility. Particularly, the decision recognised the special offices of the chairman of the board and the managing director as having the potential of being judged by higher standards of care and skill. It is curious that the court found their conduct as amounting to "gross negligence" in this case, suggesting that if their conduct had amounted to "mere negligence," they might have escaped liability.[42]

The departure by the CAMA from the Common law position must have been an attempt to introduce professionalism in the office of the company director in accordance with modern day expectations. It is true that the company director is more in the limelight today than he was decades ago. Corporate failures around the globe involving Enron, WorldCom, Vivendi, Madoff, Parmalat, Cadbury and several Nigerian banks,[43] have ensured that managers of companies are more in the spotlight now more than ever before. The failures have been partly attributed to the appointment by companies of unqualified or unskilled directors as well as the latter's outright negligence of duty.

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[41] Ibid., at 192-193.

[42] Apparently at common law, directors must be 'culpably' or 'grossly' negligent before they can be said to be in breach of the duty of care and diligence. See dicta of Romer J, Lindley MR and Rigby LJ respectively in *Lagunas Nitrate Co. vs. Lagunas Nitrate Syndicate Ltd.* (1899) 2 Ch. 392 at 418, 435 and 466 (CA). While the courts have long been unsure about exactly what 'gross negligence' means, apparently something more than what we may call 'ordinary negligence' is required. See Corkery, F.J. op.cit., p. 132.

[43] Mostly due to inadequate supervision and weak management. See Nworji, D.I., Adebayo, O. and David, O.A. (2011). Corporate Governance and Bank Failure in Nigeria: Issues, Challenges and Opportunities.*Research Journal of Finance and Accounting,* 2(2): pp. 3-4. RetrievedDecember 3, 2013, from www.iiste.org/Journals/index.php/RJFA/article/download/183/67.

Consequently, the practise in some jurisdictions today, such as the UK,[44] Australia,[45]Hong Kong[46] and South Africa,[47] is for an added subjective standard required of directors. This is suggested as having the potential to augment the objective test in order to hold directors responsible where they have special skills or qualifications not necessarily possessed by their peers, whether they happen to be executive or non-executive directors.

Granted, the CAMA improved upon the former common law by requiring a uniform objective standard. But the practice these days is to move beyond that to demand more from directors. This is because, in the past, directors didn't usually have any qualifications per se. Cases like **Re Brazillian** and **Re City** above show that they were either put their in spite of their lack of knowledge and experience or simply because of the prestige that comes with their name. But in modern times directors are often educated and hold portfolios that testify to several qualifications, with impressive resumes. Even non-executive directors, who are in office simply to monitor management, are known to have their own qualifications. They are no longer expected to be mere figure heads, as corporate codes increasingly show.[48] Added to this, the office of company director these days is often specialized or departmentalised, so that a uniform standard would be either unduly unfair or even too generous. Thus, the practice these days is to require directors to live up to their resumes, that is, deliver as much as they hold out in capabilities, apart from the general rule of living up to objective

[44] See s. 174 of UK Companies Act 2006.
[45] See s.180(1)Australia Corporations Act 2001 (as amended).
[46] See s. 465 of the new Hong Kong Companies Ordinance 2012.
[47] See s. 76(3)(c) of the South African Companies Act 2008.
[48] See generally Nigeria Securities and Exchange Commission's Code of Corporate Governance for Public Companies 2011 and the Central Bank of Nigeria Code of Corporate Governance for Banks Post Consolidation 2006.

standards.[49] This is considered a better way by addressing the issue of standard of care in relation to specializations and company types. Thus, even a non-executive director, if he has any special qualifications or experience, will be bound to put it to the use of the company. Currently under s.282, the director need not display more than the reasonable standard, unless his service contract requires it. But the law ought to allow companies to apply the subjective test to a director with more experience than "reasonable" in addition to the minimum objective standard. This will be fairer to categories of directors and also discourage embellishment of resumes.

To complement the CAMA and encourage companies to measure up to the standards of modern time, corporate codes of governance have also been periodically formulated and reviewed as guidelines by government agencies, such as the Central Bank of Nigeria (CBN) and the Securities and Exchange Commission (SEC) and these clearly demand of directors to be somewhat more of professionals. In particular, the CBN Code of Corporate Governance for Banks Post Consolidation 2006 in paragraphs 4.11, 5.3.2, and 5.3.3, requires bank directors "to be knowledgeable in business and financial matters and also possess the requisite experience"[50] and charges banks to ensure the regular training and education of board members. Under the present rules, having bank directors conducting themselves as those of **Adebayo vs. Johnson**, would be highly unlikely.

Recall that a company is not *legally* bound to appoint *competent* directors,[51] unlike the case of the company secretary provided for under s. 296 of the CAMA, wherein it is stated that a director is duty bound to take all reasonable steps to ensure

[49] See *Norman vs. Theodore Goddard* (1991) BCLC 1028; *Re D'Jan of London Ltd*.(1993) BCC 646 whose decisions informed s.174 of the UK Companies Act 2006. See also *Abbey Forwarding Ltd. (In Liquidation) vs. Hone*(2010) EWHC 2029 (Ch).

[50] Similar provisions are contained in the existing CBN Guidelines on the Appointment to the Board of Financial Institutions.

[51] Just as a director is not bound to bring any special qualification to his office. See the dictum of Neville J. in *Re Brazilian Rubber Plantation Estate Ltd.* supra.

that the secretary is a person who appears to him to have the requisite knowledge and experience to discharge the functions of a secretary of a company, with added special qualifications in the case of the secretary of a public company. Perhaps in order to make up for this, the SEC Code of Corporate Governance for Public Companies 2011 in paragraph 18.2 provides that

> *It is mandatory for all directors to participate in periodic, relevant, professional continuing education programmes in order to update their knowledge and skills and keep them informed of new developments in the company's business and operating environment. The objective of the training is to assist the directors discharge fully and effectively their duties to the company. The training shall be at the company's expense.*

The provision above is limited by a major factor: it is applicable only to public companies whose securities are listed. Private companies, even those which can pass as large companies, are not bound by the provisions of the SEC codes, although they are generally encouraged to adopt them. Although private companies are substantially more prevalent, they are not subject to the same regulations and restrictions to which public companies are.

Since there are no particular qualifications, who is a "reasonably prudent director"? The answer to this may be embedded in the phrase "in comparable circumstances." At least, this suggests that the court is entitled to take into consideration the "circumstances" of the director and the company he works for, such as the position of the director within the company, perhaps the type and extent of responsibility reposed on him and the kind of business carried out by the company. A financial company for example, may require some reasonable measure of basic accounting skills from its director, other companies. Importantly, though, it would not matter whether a director is an executive or non executive.

More decisions from Nigerian courts would have been very useful in discerning exactly how much the CAMA has achieved in deviating from the early common law position. Regrettably, this researcher has not been able to find any more directly on the director's duty of care and skill under the present law. It is debatable if there is. This may be owing to the fact that the vast majority of companies in Nigeria are private[52]—and the few that are public were previously private—and used to being run by a select group of family members and or friends, so that the tendency is for breaches of directors' duties to be settled as private matters in the boardroom or even the living room, rather than the courtroom: that is if they are ever made known.[53] Indeed, it has been suggested, and this writer tends to agree with the view, that

> *The fact patterns in actions against directors for breach of their...duties are reminiscent of stories about the "falling out of thieves." Because of the impediments in the path of a minority shareholder, attempting to initiate an action against a negligent or fraudulent director, such actions tend only to occur where there has been a family squabble between the directors themselves, or a change of control. Accordingly the court has to adjudicate upon a dispute motivated more by vindictiveness than by a desire to heighten business morality.*[54]

This pattern is observable in Nigeria. The few times management was called to order, it was usually by government agencies such as the SEC, the CBN or the Economic and Financial Crimes Commission. This was the case with companies such as

[52] Though efforts to obtain the exact number of private companies proved futile, still the Registrar General of the CAC disclosed that as at August 2014, exactly 1, 201, 068 limited liability companies were registered in Nigeria. See Bamgboye, A. (September 2, 2014). CAC to Strike Off 48, 000 Dormant Companies. *Daily Trust.*P. 45. However, the Director-General of the Securities and Exchange Commission recently disclosed in an interview that the country has just about 190 listed (public) companies. See Ogwu, M.S. (2014, April 18). We Encourage Quoted Firms to Have More Women Directors. *Daily Trust.*Business, p.22.

[53] The case of Mrs. Cecilia Ibru of Oceanic Bank mentioned infra, is a good example here. Her family used to control the bank as a private business before it went public. She was certainly used to running the affairs of the bank her way, before public agencies came in, due to the change in the status of the company from private to public. It is possible that Mrs.Ibru may have been committing similar breaches while the bank was private, and the public could not then have learnt of it.

[54]Prentice, D.D. (1967). Regal (Hastings) Ltd. vs. Gulliver: The Canadian Experience. The *Modern Law Review,* 30: 450-455, at p. 455.

Cadbury Nig. Plc, Intercontinental Bank Plc and Oceanic Bank Plc. Indeed, this partly explains the scarcity observed in local judicial decisions on the duties of directors. Thus, the prosecution of the erring directors was not under the CAMA. Rather, it was under various anti-graft instruments which defined their actions as criminal offences.[55] Even these agencies have sometimes been speculated to be mere political tools used by administrations in power to annihilate their opponents.[56]The case of Bernard Longe and First Bank, for example, a clear case of the breach of duty of care and skill, was resolved by removing the director, rather than suing him on negligence.[57] The same for the notorious Cadbury scandal whose facts were revealed only after the SEC expressed concerns regarding overstatements in the company's financial accounts.[58] Again in this case, the directors involved were simply dismissed, although it was obviously a case of the breaches of the duties of care and skill, among others.

3.4 Fiduciary Duties of Loyalty and Good Faith

A fiduciary has been described as "a person who is required to act for the benefit of another person on all matters within the scope of their relationship; one who owes to another the duties of good faith, trust, confidence and candour".[59] Evidently the company director fits this description. In fact, Section 279 is clear that he stands in a fiduciary relationship towards the company. Chief among the duties owed by directors as fiduciaries, whether as agents or trustees, are loyalty and good faith.

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[55] Examples of such legislations are the Failed Banks (Recovery of Debts) and Financial Malpractices in Banks Act 1994, the Criminal Code, and the Banks and Other Financial Institutions Act 1991.

[56] For instance, Erastus Akingbola, the former Managing Director of Intercontinental Bank has several times suggested that the CBN forcefully removed and levelled accusations against him because of the governor's affiliation with Sen. BukolaSaraki, his arch enemy.

[57]See *Longe vs. FBN Plc.* (2003) 3 NWLR (Pt. 967) 228 and (2010) All FWLR 258.

[58] See The Citizen Online. Retrieved May 5, 2014 from http://thecitizenng.com/business/cadbury-plc-heads-to-trouble-again-over-alleged-fraudulent-reporting-its-not-true-says-cadbury/.

[59] Garner, A.B. (ed.). (2004).*Black's Law Dictionary.*8th edition, West Publishing Co., United States, p. 658. See a similar definition in *Bristol and West Building Society vs. Mothew*(1998) Ch. 1.

Fiduciary duties are all pervading in the discharge, by directors, of their obligations towards the company: every task they perform and action they take must be guided by these duties, which are essentially to the advantage of the company.[60] Such is the importance of the duties that the CAMA provides guidance as to what they entail and the circumstances in which they may be expected.

3.4.1 Duties Owed to Whom?

Before discussing the director's fiduciary duties, it is apposite to first determine to whom they are owed. S. 279(1) starts off with an emphatic statement that a director stands in a fiduciary relationship *towards the company* and shall observe the utmost good faith *towards the company* in any transaction with it or on its behalf. This statement proposes that the director's fiduciary duty is one owed the company only. This follows from the issue of enforceability: only the company can enforce the duties its director owes it.[61]However, s. 279(2) immediately following, states that:

> *A director shall also owe fiduciary relationship with the company in the following circumstances: (a) where a director is acting as agent of a particular shareholder; (b) where, even though he is not an agent of any shareholder, such a shareholder or other person is dealing with the company's securities.*

The provision above seems confusing on four points. First, human nature would certainly make it near-impossible for a director to observe good faith in a transaction *with* the company. This informs the rules developed regarding conflicts of interests discussed later in this work. Second, it is hardly debatable to state that a director cannot "owe fiduciary relationship with" the company, but can only "owe a fiduciary duty to"

[60] See *Okeowo vs. Migliore* (1979) NSCC 210 at 263.
[61] Refer to section 279(9).

the company, or "stand in a fiduciary relationship towards" the company.[62]Third, if the subsection proposes to state that the director owes a fiduciary duty to the company where he is acting as agent of a shareholder, then the statement would make no sense because the company is never a fiduciary to any shareholder[63] and, if a director happened to be an agent of a shareholder, his fiduciary duties in that case would be only owed the particular shareholder and not the company, for he would not in that case be acting as its agent and for it.

Fourth, the second paragraph of the subsection as couched appears to impose fiduciary duties on a director towards any person dealing with the company's securities, whether a shareholder or not and whether he happens to be that person's agent or not. If that is the case, then the director would most certainly find it difficult to balance his primary fiduciary duty to the company as its director and then his duty to a thousand and one persons that may be dealing with that company's securities.

Osunbor has proposed that perhaps the words "a shareholder" ought to read "a director" in order for the paragraph to make sense.[64] But then, this would raise the question of whom the paragraph is referring to as "other person" for his mention would seem rather belated at this stage. Ali, on the other hand, suggests that s.279(2) can be construed to mean that a director "with" the company shall owe fiduciary duties "towards" the shareholder or other person in the instances mentioned in the succeeding paragraphs.[65] But this would suggest a double agency situation: the director would, by virtue of his office, be the agent of the company and at the same time, the agent of the shareholder. This begs the question: is the director to be taken as acting within the

[62]In other words, one cannot *owe a relationship,* but can *owe a duty* or *stand in a relationship towards* some other person.
[63] In the words of Lord MacNaughten in *Salomon vs. Salomon* (1897) AC 22, at 51, "the company is not, in law, the agent of the subscribers or trustee for them."
[64]Osunbor, O.A. op.cit.at 141.
[65]Ali, H.L. op.cit., at p.168.

authority conferred on him by the company, when he acts as agent for a shareholder? Who is his principal at the relevant time? In any case, the shareholder would then be entitled as of right to sue the company along with the director. Yet, this is not the case.[66]Besides, a director is not a trustee to persons to whom his company happens to be a trustee.[67]

Conclusively therefore, by stating in one breath that the director's fiduciary duties are owed the company as well as the shareholder and potentially, other persons, the CAMA confuses the law. This is because s. 279(9) makes it clear that only the company can enforce these duties.[68] To what end then is the law's purported mention of the director's duty to the others?

The director's fiduciary duty to the company has never been questioned, but the extension of this duty to others, has. Doubtless, a director as *agent* of a particular shareholder would stand in a fiduciary relationship towards that shareholder, even without company law stating so. This would be the natural assumption under the general law of agency. However, where the director is not in fact an agent to a shareholder, any fiduciary duties to him may rightly be called to question.

In **Percival vs. Wright**,[69] a group of shareholders in a company approached the directors with a request that the directors purchase their shares. Some of the directors did so without disclosing that a purchase of the company's undertaking was imminent, this being a piece of information which was known to them and to the other members of the board, though not to the shareholders concerned. No firm offer was ever made, and the negotiations ultimately proved abortive and the court was not satisfied that the board

[66]See s.279(9).
[67]*Percival vs. Wright* (1902) 2 Ch. 421.
[68] A member cannot here enforce any rights due to him from a director acting as his agent through derivative action under section 300 because that section would only apply if it is "the company"—or the board acting in the name of the company—that infringes upon the right of the member, not when a particular director does so.
[69](1902) 2 Ch. 421.

ever intended to sell. A shareholder brought this action against the directors asking for the sale of his shares to be set aside for non-disclosure.

Eady J. held that the directors are not trustees for the individual shareholders and may purchase their shares without disclosing pending negotiations for the sale of the company, and even though the price being offered for the undertaking was substantially more than they paid on the purchase. To hold otherwise would mean that they could not buy or sell shares without disclosing negotiations, a premature disclosure of which might well be against the best interests of the company. There was no *unfair dealing* under the circumstances. Accordingly, the shareholder could not have the transaction set aside for non disclosure.

It is noteworthy that in arriving at this decision, the court stressed the special circumstances of this particular case. It was especially significant that the initial approach in the matter was made by the shareholders.[70] It is therefore possible that the court would have decided otherwise, had the directors been the ones who approached the shareholders.[71] Moreover, the directors would have had to account to the company, having used company information to their own use.

However, in spite of the decision above, there appears to be a duty to shareholders concerning any advice given by directors to shareholders regarding the acquisition or rejection of a takeover bid.[72] In **Gething vs. Kilner**,[73] it was decided that in a takeover situation, the directors of the 'victim' company owe "a duty towards their own shareholders which...clearly includes a duty to be honest and a duty not to mislead" as by suppressing, for instance, professional advice recommending rejection, and that

[70] Ibid. at 426-427.
[71] Birds, J. et al. (2011).*Boyle and Birds' Company Law.*8th edition, Jordan Publishing Limited, Bristol, p. 628.
[72] Wild, C. and Weinstein, S.op.cit.at345.
[73] (1972) 1 WLR, 337.

the court might grant an injunction where this had happened, to prevent the bid from getting through.[74]

The courts do not also entirely rule out a fiduciary or other duty owed to individual shareholders by the directors, where, on the facts of a case, the directors place themselves as against the shareholders individually in a legal relationship such as agency.[75] This may arise, for example, where the shareholders authorise the directors to sell their shares on their behalf to a potential takeover bidder, as was the case in **Allen vs. Hyatt**.[76] There, the directors induced the shareholders to give them options for the purchase of their shares so that the directors might negotiate a sale of the shares to another company. The directors used the options to purchase the shares themselves and then resold them at a profit to the other company. The Privy Council held that, under the circumstances, the directors had made themselves agents for the shareholders and must consequently account for the profit made.

A major disadvantage has been noted in this agency arrangement, though.[77] It was held by the House of Lords in **Briess vs. Woolley**[78] that where shareholders employ the directors to negotiate a sale of their shares, the shareholders will be vicariously liable in damages to the purchaser as principals, if the directors fraudulently misrepresent the state of the company's affairs to the purchaser.

Aside from clear agency situations, the New Zealand Court of Appeal has considered the doctrine of a "special factual relationship" to cover situations where the directors are not in fact agents of the shareholders. Thus, in **Coleman vs. Myers**,[79] the court found that a fiduciary duty of disclosure arose, even in the absence of agency, in

[74]Ibid. per Brightman at 341.
[75]Davies, L.P. and Worthington, S.op.cit.at 507.
[76](1914) 30 T.L.R. 444, PC.
[77]Wild, C. and Weinstein, S.op.cit.at 345.
[78] (1954) 1 All ER 909
[79](1977) 2 N.Z.L.R. 225, NZCA.

the case of a small family company where there was a gross disparity of knowledge between the directors and the shareholders and where the shareholders of the company had traditionally relied on the directors for information and advice. The court clarified that whether a duty existed at all depended on "information and advice, the existence of a relationship of confidence, the significance of some particular transaction for the parties and the extent of any positive action taken by, or on behalf of, the director(s) to promote it."[80]When the directors negotiated with the shareholders for the purchase of their shares and, therefore, were clearly not acting on behalf of the shareholders, they were nonetheless held to be subject to a fiduciary duty of full disclosure of relevant facts about the company to the shareholders.

While approving the decision above, Mummery L.J. of the English Court of Appeal, in the case of **Peskin vs. Anderson**,[81] had occasion to distinguish between fiduciary duties owed by directors to the company which arise out of the relationship between the director and the company, and fiduciary duties owed to shareholders which are dependent upon establishing "a special factual relationship between the directors and the shareholders in the particular case".[82] Each case must therefore be decided based on the facts.

From the report of the Nigerian Law Reform Commission, s. 279(2) appears to be an attempt to codify the foreign decisions discussed above.[83] If that is the case, then, as earlier pointed out, the CAMA has further confused, rather than clarified, the statement of the law. However, it is important to note that were a situation such as that in **Percival vs. Wright** to occur in Nigeria, it is likely to be decided in much the same way, for it would not amount to *insider dealing* which would have quite easily been

[80]Supra at p.325.
[81](2001) 1 B.C.L.C. 372.
[82]Ibid. at 379. See also *Platt vs. Platt* (1999) 2 BCLC 745.
[83]See Nigerian Law Reform commission Report (1988) Vol. 1, p.209-211.

addressed under s. 111 of the Investment and Securities Act 2007.[84] This is because the case of *Percival* involved private dealings in shares, while the latter section is relevant only where the securities of the company are offered to the public for sale or subscription. Under that law, a director qualifies as "insider" and is therefore subject to the restrictions stated therein, when he deals in securities.

Curiously, s. 279(4) states that, while at his job, "the matters to which the director of a company is to have regard in the performance of his functions include the interests of the company's employees in general, as well as the interests of its members." To "have regard" means to appreciate the worth of something,[85] or to show attention or consideration towards something.[86] Nowise does it mean "to owe obligation or duty". Therefore, the intention of the law must be taken to mean *to show consideration* to the interests of employees and members in general, while the ultimate duty of the director is still as set in s. 279(3): the best interests of the company as a whole.

However, it can be strongly argued that owing a duty to the company is *in fact* owing a duty to "its members" collectively, for, although the company is considered as having a separate and distinct personality from those of its members,[87] it is in fact for the ultimate benefit of the members collectively, whose "association" initially formed the company,[88] that the company exists. According to Berle and Means,

> *...where powers are conceded to the management...to act for the corporation as a whole, the obvious...assumption is that these powers are intended to be used only on behalf of all. They are distinctly not intended to be granted for the purpose of benefiting one set of participants as against*

[84]Act No. 29, 2007.
[85]Encarta Dictionaries (2009).Microsoft Encarta Premium DVD.
[86]Longman Dictionary of Contemporary English, op.cit.at 1380.
[87]*Salomon vs. Salomon & Co. Ltd.* (1897) A.C. 22.
[88] Refer to Section 37.

another. To do so would be to violate every intendment of the whole corporate situation.[89]

This argument can further be buttressed by the fact that the members in a general meeting can set the motion for the company to enforce the director's duties.[90] Therefore, the law to the extent of juxtaposing "employees" and "members" here as having comparable rights in the director's duty to have regard, is misleading, although, as will be discussed presently in this work, there are strong opinions outside of company law that tend to suggest otherwise.

3.4.2 In Whose Interests and for whose Benefit Should Directors Manage the Company?

The fact of the company being asked to have regard to the interests of employees through its directors, revives the rather ancient debate between Berle[91] and Dodd[92] regarding the ultimate objective of the company: in whose interests and for whose benefit is it to be managed?[93] The ancient and prevailing objective of business obviously is to create the most value for the business owner. But the company has special attributes that set it apart from any other type of business arrangement. The decision in **Salomon vs. Salomon & Co. Ltd.**[94] has already established the distinctive identity of the company as being separate from those of its members or shareholders or any person associated with it for that matter. The question is: who, in fact, is the "owner" of the

[89]Berle, A.A., and Means C.G. (1932).*The Modern Corporation and Private Property*. The Macmillan Company, New York, p. 274.
[90]Aside from the fact that a single member can also indirectly enforce directors' duties through the medium of derivative action provided in Sections 301, 303 and 311.
[91]Berle, A.A. (1931). Corporate Powers as Powers in Trust.*Harvard Law Review,* 44: 1049; Berle, A.A. (1932).For Whom Managers are Trustees: A Note. *Harvard Law Review*, 45: 1365; Berle, A.A., and Means C.G., op.cit.
[92] Dodd, E.M. (1932).For Whom are Corporate Managers Trusties?*Harvard Law Review*, 45: 1145; Dodd, E.M. (1935).Is Effective Enforcement of the Fiduciary Duties of Corporate Managers Practicable?*University of Chicago Law Review*, 2: 194.
[93]Berle and Means considered this essentially the question: "who should receive the profits of industry?" See Berle, A.A., and Means C.G.,op.cit. at 333.
[94](1897) A.C., 22.

corporation? It was decided in **Macaura vs. Northern Assurance**[95] that "the corporator, even if he holds all the shares, is not the corporation..."[96] Conclusively, therefore, the company has no owner as even the shareholder or member, does not own the company, but at the most, only has a *transferableinterest* in it.[97] It is a fact that company law often requires directors to act in the best interests of the company.[98] But since *the company* is an abstract—and in order to lend some practicality to the rule—it has been held that the interests of the company is akin to the interests of all its members.[99]

Berle likened the corporation to the *private property* of its shareholders.[100] Therefore, "all powers granted to a corporation or to the management of a corporation are necessarily and at all times exercisable only for the ratable benefit of all the shareholders as their interest appears."[101] He argued that directors should not, as managers of companies, have any responsibilities other than to the shareholders of their companies, for whom money was to be made.[102] In essence, shareholders are like *owners* of the corporation, while directors managing the corporation are *trustees* and *agents* for the owners. In the words of Berle and Means,

> *Wherever one man or a group of men entrusted another man or group with the management of property, the second group became fiduciaries. As*

[95](1925) A.C. 619.
[96]Per Lord Wrenbury, at page 633.
[97] See *Short vs. Treasury Commissioners* (1948) 1 KB 116 at 122 where Lord Justice Evershed of the English Court of Appeal refused the supposition that shareholders were the owners of the company.
[98] See for instance s. 8.30(a) of the United States Model Business Corporation Act; s. 181(1) Australian Corporations Act 2001; s. 122(1) (a) Canada Business Corporations Act 1985; s. 172(1) UK Companies Act 2006; s. 279(3) CAMA.
[99] In *Brady vs. Brady* (1988) B.C.L.C. 20 at 40, C.A., Nourse L.J also pointed out that "the interests of a company as an artificial person cannot be distinguished from the interests of the persons who are interested in it."See also Birds, J. *et al. op.cit. at*pp.634 and 636 andalso Nigerian Law Reform Commission Report (1988) Vol. 1, p.210.
[100] See Berle, A.A., and Means C.G., op.cit. at 334.He believed that owners ought to receive the profits of the corporation because they acquired ownership of the corporate venture and are the rightful benefactors of all corporate economic surplus to the exclusion of all non-owners. See also Stewart, F. (2011).Berle's Conception of Shareholder Primacy: A Forgotten Perspective for Reconsideration During the Rise of Finance. *Seattle University Law Review,*34:1457-1499, at 1470.
[101]Berle, A.A.(1931). Op.cit.,at p. 1049.
[102] Ibid.

> *such, they were obliged to act conscionably, which meant in fidelity to the interests of the persons whose wealth they had undertaken to handle. In this respect, the corporation stands on precisely the same footing as the common law trust.*[103]

Dodd, on the other hand, argued that the managers' duty ought to be extended to other stakeholders. From his perspective, managers were granted many freedoms, whether through law or factual circumstance, to conduct business in a manner that would not necessarily maximize profits.[104] He conceded to Berle that managers owed a fiduciary duty to the shareholders not as individuals but only to shareholders as one of many groups.[105] Yet, management must be seen to be serving the best interests of the corporation as a whole. Thus, although the sole function of the corporation was still profit making for its investors, managerial discretion must be liberal enough to take into consideration the interests of other groups such as employees, customers, creditors and others, even at the expense of maximizing profits.[106] He saw Berle's conception of the fiduciary duty of the directors solely to the shareholders as having the potential to create a serious obstacle to achieving socially responsible managers.[107] He further argued that to promote socially responsible behaviour, corporate managers (directors) need to be the guardians of all interests that the corporation affected, not just those of the shareholders.[108]

Berle later countered this corporate responsibility argument as being naively trusting of corporate managers.[109] He conceded to Dodd that managers did wield immense government-like power over society, but argued that they did not thereby regard themselves as stewards of society and did not assume social responsibility.

[103]Berle, A.A., and Means C.G., op.cit.at 336.
[104] Dodd, E.M. (1932) op.cit.,at p.1147.
[105]Ibid., note 139 at p.1146.
[106] Ibid. at 1147-1148.
[107]Ibid. at 1162.
[108]Ibid. at 1161.
[109]Stewart, F. op.cit.at 1482, citing Berle, A.A. (1932). Op.cit. at p.1367.

Besides, no mechanism existed to enforce the applications of what he called Dodd's "pseudo-theory of the corporation."[110] He further countered that if the exclusive fiduciary obligation of mangers to shareholders were to be ignored, then the management and *control* would become "for all practical purposes absolute"—resulting in greater *corporate irresponsibility*. Therefore, until such time as Dodd (or any others who sympathized with the noble manager) was prepared to offer a "clear and reasonable enforcement scheme of responsibilities," emphasis would have to be placed on the fact that the corporation's sole purpose was to make profit for its shareholders because there existed no other legal control over corporate power, however imperfect it may be.[111]

In the end, Dodd conceded the debate to Berle, admitting

> *I was rash enough to suggest that our law of business corporations. . . might develop a broader view which would make the proposition that corporate managers are, to some extent, trustees for labour and for the consumer more than meaningless rhetoric. The legal difficulties which were involved were clear enough, as Mr. A. A. Berle was quick to point out.*[112]

Two prominent competing management ideas later emerged from the foregoing discourses: the shareholder primacy theory and the stakeholder theory. Shareholder primacy refers to the idea of putting the interests of the shareholders first before any other group or factors, so that the corporation served no public purpose, unless such purposes furthered the financial interests of the shareholders.[113] According to the proponents of this theory, the social responsibility of business is "to use its resources and engage in activities designed to increase its profits, so long as it...engages in open

[110]Berle, A.A. (1932) op.cit.at 1367.
[111]Stewart, F. op.cit.at 1483, citing Berle, A.A. (1932).Op.cit., note 164at 1367.
[112]Stewart, F. op.cit.at 1490, citing Dodd in a book review inDodd, E.M., (1942). Book Review, *University of Chicago Law Review,*9: 538at 546 (1942) (reviewingDimock, M.E.and Hyde, K.H. (1940).*Bureaucracy and Trusteeship in LargeCorporations*.
[113] Byrne, P.T. (2010). False Profits: Reviving the Corporation's Public Purpose.*UCLA Law Review Discourse*, 57: 25-49, at 36.

and free competition without deception or fraud."[114] The view that managers should focus primarily on shareholder interests has been closely tied to the shareholder primacy norm (SPN), which is the part of the manager's legal fiduciary duty that requires managers to make decisions on behalf of the corporation that furthers the interests of shareholders.[115] Since the interest of shareholders is to maximize return on investment, SPN would result in shareholder value maximization (SVM).[116]

Early in 1919, in the case of **Dodge vs. Ford Motor Co**.,[117] Justice Orlander of the Supreme Court of the United States state of Michigan gave what to date is considered the most direct and explicit endorsement of shareholder primacy in legal records:[118]

> *A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end and does not extend to a change in the end itself, to the reduction of profits or to the non-distribution of profits among shareholders in order to devote them to other purposes.*[119]

Evidently, courts in the past had a somewhat narrow idea of what the corporation was set to achieve and how it was to achieve it. It would seem that even today, the Anglo-American jurisdiction, comprising the UK, USA, Canada, New Zealand, Australia and a great number from the British Commonwealth, has its corporate

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[114]Friedman, M. (1962).*Capitalism and Freedom.*University of Chicago Press, p. 133. See also Friedman, M. (1970, September 13). The Social Responsibility of Business is to Increase Its Profits. *The New York Times Magazine.*Retrieved May 24, 2014 from http://www.umich.edu/~thecore/doc/Friedman.pdf.The popular U.S. court decision in *Dodge vs. Ford Motor Co*. (1919) 170 N.W. 668 clearly supported this ideology.

[115]Ronnegard, D. and Smith, N.C. (2011).*Shareholders vs. Stakeholders: How Liberal and Libertarian Political Philosophy Frames the Basic Debate in Business Ethics.*Faculty and Research Working Paper, Insead Social Innovation Centre, France, p. 3.

[116]Ibid. at 4.

[117] (1919) 170 N.W. 668

[118] Ralph, G. (2012).*BCE and the Shareholder Primacy Paradox: A Theory at War with Itself.*(LL.M. thesis University of Toronto, Canada) p. 15.Retrieved September 23, 2013 from https://tspace.library.utoronto.ca/bitstream/1807/33219/1/gill_ralph_201211_LLM_thesis.pdf.

[119]*Dodge vs. Ford Motor Co*. supra at 685.

structure designed to ensure that corporations work primarily in the interest of shareholders.[120] However, it is pertinent to note that in none of the company laws of these jurisdictions are directors tasked to specifically consider *only* the interests of the shareholders:[121] instead, it is the allocation of corporate power and legal and proprietary rights that results in a situation amounting to shareholder primacy. This is obvious from the fact that the shareholders in the general meeting have the statutory power to appoint and remove directors; decide their remuneration and withdraw their funds from the enterprise, thereby having the potential to influence directors in their decision making. Thus, although directors are not *legally* mandated to consider *only* the interests of shareholders, the latter group has been statutorily armed to ensure that the directors do just that. Conclusively, the legal power of shareholders to vote for the board of directors and their remuneration helps to perpetuate the SPN as a social norm, not necessarily as a principle of law likely to be upheld in court.[122]

While the SPN has enjoyed the advantage of corporate law,[123] its advocates argue that this is because management is thereby more focused in achieving the main objective of the company. It is believed that it is much more difficult for directors to make excuses for poor performance when they are being held to account by

[120]Anderson, M. *et al.* (2011).*Evaluating the Shareholder Primacy Theory: Evidence from a Survey of Australian Directors.*Corporate Governance and Workplace Partnership Project, Faculty of Law, University of Melbourne, Australia, p. 1. Retrieved September 6, fromhttp://www.law.unimelb.edu.au/files/dmfile/Evaluatingtheshareholderprimacytheoryevidencefromasurveyof_Australian_directors__20_11_07_2.pdf. See also Ronnegard, D. and Smith, N.C. op.cit., atpp.6-7.

[121]On the contrary, in most of the company laws following the Anglo-American corporate regulatory system, directors are usually required simply to act "in good faith in the best interests of the company". See for example s. 8.30(a) of the United States Model Business Corporation Act; s. 181(1) Australian Corporations Act 2001; s. 122(1) (a) Canada Business Corporations Act 1985; s. 172(1) UK Companies Act 2006; s. 279(3) CAMA.

[122]Ronnegard, D. and Smith, N.C., op.cit., atp.8. The court would most likely let the directors get away with any business judgment exercised in good faith in the interests of the company, regardless of the outcome, unless discovered to have been arrived at mala fide.

[123]Owing to the fact of the critical powers and rights usually available to shareholders under corporate law.

shareholders.[124] However, the SPN has been criticized as resulting in directors focusing mostly on share price maximization, often leading to short-term[125]—rather than long-term—success, by neglecting the contributions of groups vital to the overall success of the company (stakeholders) and employing business practices that are often unethical, immoral or even illegal, thereby ignoring the duties the company owes to society as a corporate citizen. In other words, the avid pursuit of share price maximization may lead managers to grossly violate stakeholder interests.[126]

But Jensen,[127] an avid shareholder primacy advocate explains that wealth maximization does not mean that firms should completely neglect stakeholders. Rather than ignore its stakeholders, what a shareholder-driven company does is invest resources to benefit each stakeholder to a point where the additional benefits to the company exceed the additional cost.[128]

On the other hand, stakeholder theory proposes the idea that the corporation as an entity, acting through its directors, owes a duty to consider the interests of all its stakeholders. "Stakeholder" has been broadly defined as any group, individual or factor that can affect or be affected by the realization of an organization's purpose.[129] By this definition, therefore, shareholders, the company, employees, customers, suppliers, creditors, the community, the environment, and even the country, all make the list. The theorists of this *pluralist* business ideology believe that any business, large or small, is

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[124] Jensen, M.C. (2002).Value Maximization, Stakeholder Theory and the Corporate Objective Function.*Business Ethics Quarterly,*12: 235-256. Retrieved September 10, 2013, from www.hbs.edu/faculty/Pages/download.aspx?name=00-058.pdf.

[125] Or "short-termism," variously defined as "seeking short-term gain to the exclusion of long-term achievement." See Mullins, D. In: Jacobs, M. (1991).Short-Term America.*Harvard Business School Press*, Boston; and "foregoing economically worthwhile investments with longer-term benefits in order to increase reported earnings for the current period." See Grinyer et al. (1998).Evidence of Managerial Short-Termism in the UK.*British Journal of Management, 12:*13 at p.15.

[126]Colinger, D.O. (1995).Managerial Roles and Ethical Behaviour.*Financial Practice and Education*, 5: 50.

[127]Jensen, M.C. (2002) op.cit.

[128] Jensen, M.C. (1989). *The Evidence Speaks Loud and Clear,* vol. 67(6) Harvard Business Review, 186-188, at 186.

[129]Freeman, R.E. *et al.* (2010). *Stakeholder Theory: The State of the Art*.Cambridge University Press, New York, p. 26.

about creating value for "those groups without whose support the business would cease to be viable and since every business is concerned at some level with relationships between financiers (including shareholders), customers, suppliers, employees and communities, these groups can be considered the "primary" or "definitional" stakeholders.[130]

Each of the stakeholder groups has a special "stake" in the company: shareholders and financiers undoubtedly have a financial stake in the form of stocks, bonds, etc. upon which they expect favourable financial returns; employees have their jobs and usually, livelihood at stake: in return for their labour, they expect security, wages, benefits and meaningful work and in return for their loyalty, the company is expected to provide for them and carry them through difficult times; supplies made by suppliers determine the products' final quality and in return, the company becomes a customer to the suppliers and so, vital to the suppliers success and survival; customers exchange resources in return for benefit in the form of products and services; and communities, for allowing companies to build facilities in their domain, thereby exposing themselves to many kinds of hazards, are entitled to expect those companies to live up to the expectation of good corporate citizenship and in return, benefit from the tax base and economic and social contributions of the company.[131]Indeed, the notion that the corporation is like a "citizen" and therefore, has to conform to "public notions of citizenship" was earlier put forward by Dodd.[132]

No stakeholder stands alone in the process of value creation. The stakes of each stakeholder group are multifaceted and inherently connected to each other in terms of

[130]Ibid.
[131] Freeman, E.R. *et al,* op.cit., atpp.24-25 and Freeman E.R. (2001).Stakeholder Theory of the Modern Corporation.*General Issues in Business Ethics*, 38 at 42-43. Retrieved September 8, 2013, fromhttp://academic.udayton.edu/lawrenceulrich/Stakeholder%20Theory.pdf
[132]Dodd, E.M. (1932) Op.cit. at p.1148.

harms and benefits as well as rights and duties,[133] which makes balancing all the more crucial. While positing that "stakes" require action of a certain sort, Freeman acknowledged that "competing stakes" require methods of resolution.[134]Yet, stakeholder theory prohibits any undue attention to the interests of any single constituency,[135] although admits that there would be times when one group benefits at the expense of the others.[136] Therefore, the notion of *equality* seems appropriate for a norm representing stakeholder theory because if stakeholders are not equal in the eyes of management, one group must be primary[137] and this would simply result in another *primacynorm*.

A closely associated concept is corporate social responsibility (CSR), which posits that the private corporation has responsibilities to society that goes beyond the production of goods and services at a profit so that the corporation has a broader constituency to serve than shareholders alone.[138] It is believed that there are social obligations that push the company to go beyond the requirements of the law.[139] However, Friedman, a foremost SPN advocate, questions how "business", an inanimate object, can be constrained by social responsibilities.[140] According to him, corporations possess neither the authority nor the moral right to divert shareholders' profits for the welfare of the general public. He argues that

> *Managers are merely agents of the stockholders, and thus have no right to spend or give away corporate*

[133]Freeman, E.R.*et al*, op.cit.at 27.
[134] Freeman, E.R. Op.cit., at p.41.
[135]Donaldson, T. and Preston, L.E. (1995).The Stakeholder Theory of the Corporation: Concepts, Evidence and Implications.*Academy of Management Review*, 20(1): 87.
[136]Freeman E.R. op.cit.at 44.
[137]Ronnegard, D. and Smith, N.C., op.cit. at 16.
[138]Buchholz, R.A. and Rosenthal, S.B. (2002).*Social Responsibility and Business Ethics*. In: Frederick, E.R. (Ed.) A Companion to Business Ethics, Blackwell Publishers, Massachusetts, 303-322, at 303, cited in Ronnegard, D. and Smith, N.C. op.cit. at p. 4.
[139] Davis, K. (1973).The Case for and Against Business Assumption of Social Responsibilities.*Academy of Management Journal*, 16(2): 312-322, at p.313.
[140]Friedman, M. (1970).*A Friedman Doctrine: The Social Responsibility of Business is to Increase Its Profits.* New York Times Magazine, September 13, 1970 atp.33.Cited in Grossman, A.H. (2005).Refining the Role of the Corporation: The Impact of Corporate Social Responsibility on Shareholder Primacy Theory.*Deakin Law Review*, 10(2): 572-596, at p.574.

> *monies except in the interests of increasing shareholder wealth…any stockholder is free to use his dividends to support any worthy causes he may choose, but the choice should not be made for him by a company president who may not share either his values or priorities.*[141]

Proponents of CSR and stakeholder management theory, in contrast, find fault with the proposition that corporations owe no societal obligations or that shareholders should be given the most importance in managerial decisions because they are "the only constituency of the corporation with a long-term interest in its survival",[142] since shareholders can easily sell their shares at any time and reinvest in another company. In contrast, employees—particularly the ones that have acquired firm-specific skills—would find it relatively more difficult to change employers; customers could lose an essential source of supply and local communities would be varyingly adversely affected if a company ceases to exist.[143]

However, stakeholder theory has been criticised not only for tampering with the rights of the capital owner, but also for its inability to provide some guide as to balancing competing interests.[144] Some of its proponents suggest that where interests conflict, the executive must find a way to rethink the problems so that the various adverse interests can go together and so that as much value as possible is created for all stakeholders.[145] Thus, they admit that it is not always going to be easy to accommodate all stakeholder interests.

Proponents of SPN argue that corporate law does not prevent directors from considering the interests of other stakeholders apart from the shareholders. But stakeholder advocates believe that, although the discretion of decision-making should lie

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[141] Ibid.
[142] Jensen, M.C. op.cit.at 187.
[143] Freeman *et al,* op.cit. at 129.
[144] Keay, A. (2007).Tackling the Issue of the Corporate Objective: An Analysis of the United Kingdom's 'Enlightened Shareholder Value Approach.*Sydney Law Review,* 29: 577-612, at p.611.
[145] Freeman, *et al*, op.cit. at 28

with management together with stakeholder representatives,[146] unless these representatives are given real power, such as an equal right to vote, ultimately it would still result in a situation of shareholder primacy, even where the decision is informed by the different interests in a company.[147]

In other words, SPN theorists do not deny that a company should consider the interests of its stakeholders. However, it should consider them only to the extent that they further its purpose or interests:[148] essentially as a means to an end and not an end in itself. But this is precisely what stakeholder advocates resent. Freeman is adamant that "each of these stakeholder groups has a right not to be treated as a means to some end and therefore must participate in determining the future direction of the firm in which they have a stake."[149] Companies in some jurisdictions, particularly Continental Europe and Japan, have a two-tier board system comprising employees and management. However, the former is at most merely advisory.[150]

In view of the foregoing, and considering the provisions of s. 279(3), the CAMA undoubtedly belongs to the Anglo-American jurisdiction, which supports the idea that directors should act, first and foremost, in the best interests of the company. Although subsection (4) allows other possible stakeholder interests including the company's employees, it is clear that the latter group has no means of enforcing that provision in view of their ouster by subsection (9). Here, one would have to agree with Ogbuanya, who dubbed the section "a mere pious declaration."[151] While discussing a similar provision in s.309 of UK's Companies Act of 1985, Keay acknowledged it was a "lame

[146]Mele, D.*Corporate Social Responsibility Theories.* In Crane A. *et al* (Eds.) (2008).The Oxford Handbook of Corporate Social Responsibility, Oxford University Press, Oxford, 47 at 48.
[147]Ronnegard, D. and Smith, N.C., op.cit. at 16.
[148] See in particular the decision of Bowen L.J. in *Hutton vs. West Cork Railway* (1883) 23 Ch. D. at 673
[149]Freeman E.R. op.cit.at 39.
[150] See Farrar, H.J. (2008). *Corporate Governance: Theories, Principles and Practice*. Oxford University Press, England, pp.23, 34 and 35.
[151]Ogbuanya, N.C.S., op.cit. at 337.

duck" provision owing to the fact that hardly any cases had been reported regarding its breach because of the obvious difficulty employees would encounter in any such action.[152] The company's members, on the other hand, may possibly use their rights, including the right to attend and vote at meetings[153] appoint and remove directors,[154] and institute derivative actions,[155] to ensure that directors in fact consider *their* interests as paramount. Whether or not they in fact utilize these opportunities, is a discussion for another day. Still, nothing *legally* stops the directors from taking into consideration a wide range of stakeholder interests. If need be, they can always justify their actions under s. 279(3),[156]though their actions may also be defeated if analysed under the principles in the same section.[157]

Although the CAMA has made some provision for the company's employees as stakeholders so that the issue of their welfare is included in the directors' report, and they may share in the company's profit and can even possibly be compensated upon cessation or transfer of the business,[158] these provisions nowise make them equals with members in the company because of the critical issue of the absence of voting power. In the absence of *equality*, therefore, there is *primacy* to the advantage of the members, under the law.

There appears to be some logic in the proposition that managing the company strictly on shareholder primacy principles would sooner bring the company down than assure its long-term success. This is because the most obvious interests of shareholders

[152]Keay, A. op.cit.at 593.
[153]Ss. 81 and 227.
[154]Ss. 248 and 262.
[155]Ss. 301, 303 and 310.
[156] This is because, as earlier stated, the court would most likely let the directors get away with any business judgment exercised in good faith "in the interests of the company," regardless of the outcome.
[157] See *Re W & M Roith Ltd.* (1967) 1 W.L.R. 432., where the court ruled that making provision for the widow of a former employee was not binding on the company because it was not ultimately to the company's benefit.
[158]Ss. 342(5), 384 and 566, respectively. In particular, s.566 essentially rejects the decision in *Parke vs. Daily News Ltd.* (1962) Ch. 927, wherein the court held that the defendant company had no power to make redundancy payments to its employees.

is profit: if the directors were to look only to achieving that, the overall business objective and long term success of the company may be jeopardised in a bid to make shareholders happy by declaring a dividend at every turn. But then on the other hand, if directors were to be made to consider a broad picture of the various, albeit often conflicting, interests of the company's diverse stakeholders, including the shareholders, there is the nagging problem of deciding whose interests among all the stakeholders, should take precedence in the event of a clash in any particular case? Finding a balance, when directors are faced with this situation, is the one thing that seems elusive, even for stakeholder theorists. Should stakeholders as well be armed with voting power within the corporation, this would significantly alter the whole theory of capitalism[159] and, by inference, the corporation, since companies would then be obliged to play an active role in the pursuit of wider social policy goals, over and above their own business objectives.[160] The capital owner would cease to be "king", so to speak.

The fact remains that only the company can as of right legally enforce its directors' fiduciary duties. But then, who is *the company?* If the directors were to abandon the interests of the company in favour of the interests of the shareholders—say, by declaring a dividend instead of recapitalizing to buy some much needed state-of-the-art machinery or employing better skilled labour—who would bring the directors to book in such a situation? Obviously, not the shareholders in whose ultimate favour the directors might have acted, and definitely not the directors themselves who may stand to be indicted for breach of duty. Unfortunately, these are the only "organs" through which the company might have acted in order to redress the "wrong".[161] Under the circumstances, therefore, it is hardly surprising that to date, there has been no report of an action to enforce the employees' aspect of s. 279(4).

[159]Which posits that the owner of capital has the sole right of control over its use and proceeds.
[160]Davies, J. op.cit.
[161] See s. 63(3) & (5)(b).

In Nigeria, outside of corporate law, there are several ways a company's stakeholders could possibly protect their stakes in the corporation. Apart from the all-pervading contract law, there is the Consumer Protection Council Act[162] for consumers; the various labour and industrial laws for employees; and many tax and environmental laws that host communities can fall back on to, albeit indirectly, enforce any rights they may have against the company.

In sum, it appears that, unless company law is prepared to grant full voting rights to the stakeholders of the company, stakeholder theory is just that: theory. It would be very difficult to effectively put it into practice. However, the interests of the company's stakeholders would continue to be addressed within the existing corporate legal framework, to the extent that they have a bearing on the ultimate interest of the company *for the benefit of its members*and also through a corpus of relevant statutes outside of corporate law.

Having addressed the preliminary questions regarding to whom directors owe their fiduciary duties, as well as in whose interests they in fact manage the company, this work presently considers the statutory expression of those duties and the court decisions expounding them.

3.5 Duty to Act in the Best Interests of the Company and for Proper Purpose

A popular view[163] holds that the duty of the director is ultimately to the company because his allowances and or remuneration is paid by the company and whenever he is found wanting in his obligations, it is the company and only the company that can call him to order, through the instrumentality of the board of directors or the general meeting. It is the authority given him by the company via his appointment to office that

[162] Cap C25, Laws of the Federation of Nigeria 2004.
[163] Attributed to Adolf Berle and proponents of shareholder primacy theory, generally.

gives legitimacy to any of his acts. In essence, his allegiance lies with the company. Therefore, to ask him to act bona fide for the benefit, only, of the company and its purpose, seems to be in order.In order for the director to act bona fide in the best interests of the company, he would need to use the powers at his disposal for the proper purpose and not a collateral purpose. Before considering the legal interpretation of the above principles by the courts, it is pertinent to first discover how successful or otherwise the CAMA has been in expressing this duty and its allied principles.

S. 279(1) starts off by stating, inter alia, that a director "...shall observe the utmost good faith towards the company in any transaction with it or on its behalf." Good faith refers to "a state of mind consisting in (1) honesty in belief or purpose, (2) faithfulness to one's duty or obligation, (3) observance of reasonable commercial standards of fair dealing..., (4) absence of intent to defraud or to seek unconscionable advantage."[164] It is especially in senses 2 to 4 that the Act seeks to bind the director. In other words, "good faith" is the proper mindset of a fiduciary, which a director is and therefore, it is the first and main duty that must be considered when examining the conduct of any company director, before an analysis is undertaken of any other duty (whether statutory or otherwise).

In spite of the fact that s. 283 considers directors to be trustees of the company's moneys, properties and their powers, the phrase "in any transaction with it" in s. 279(1) suggests that there are instances where the director may in fact transact *with*, rather than *for* or *on behalf of*, the company, and this would be consistent with other sections within the CAMA which allow this under certain circumstances.[165] However, where he does transact with the company, he does not do so in his capacity as its director but an outsider, although certain restrictions apply to him because he is the company's director.

[164] Garner, A.B. op.cit. at713.
[165] See ss. 277 and 284, for example.

In any case, the bulk of the transactions a director is likely to be involved in would most certainly be *on behalf of*, rather than *with*, the company, though the Act demands of the director to observe good faith in both situations, difficult as that might seem in the latter situation.

S. 279(3) gives a further directive that

> *a director shall act at all times in* ***what he believes*** *to be the best interests of the company as a whole so as to preserve its assets, further its business, and promote the purposes for which it was formed, and* ***in such manner as a faithful, diligent, careful and ordinarily skilful director would act*** *in the circumstances*. (emphasis added)

From the tenor of the law above, asking the director to act in *what he believes* to be the best interests of the company, is giving him room to exercise his subjective judgment. On the other hand, asking him to discharge this obligation *in such a manner as a faithful, diligent, careful and ordinarily skilful director would act*, is akin to the law taking back with the left hand, what it had just offered the director with the right hand. In other words, ultimately, his actions are still to be judged with the scale of objectivity. It is therefore not clear from the wording whether the intendment of the Act here is to truly give the director independence and opportunity to rely on his subjective judgment in business matters. In any case, as discussed above,[166] a director is already required to show *reasonable* skill and care in the discharge of *all* his functions, so that his actions and decisions would conclusivelyalso be judged by those standards of reasonableness. A fortiori, the director's duty of care and skill and his fiduciary duties of loyalty and good faith under the CAMA, are measurable by different standards: subjective in the former and objective in the latter. Thus, if the Act intends, by the second arm of s.279(3), to

[166] Please refer to **3.2** in this work.

thereby re-state the director's duty of care and skill, this would simply be a repetition of the duty appropriately and adequately captured in s. 282.

As for *furthering its business* and *promoting the purpose for which the company was formed*, this is most likely alluding to the business clause of the company contained in its memorandum of association. Therein is stated the business or objective for which the company is formed and, in line with the *ultra vires* rule, a company ordinarily has power to go into only that business recognised by its memorandum, or at least, not contrary to it.[167] The actions of the directors must be seen to be along those lines.

While s. 279(3) refers to "interests of the company", subsection (4) provides that "the matters to which the director of a company is to have regard in the performance of his functions include the interests of the company's employees in general as well as the interests of its members." By mentioning "interests of the company" and "interests of the members" in different subsections, the Act implies that these are not the same. This work earlier argued[168] that the law, by placing employees and members in the same category, is misleading. Common law normally identified the interests of the company with those of the members, current and future, as appropriate.[169] If the members invest their money in the company and, depending on whether the company does well or not, get favourable returns or suffer losses on their investment, and like the company, also have a statutory forum in which to decide matters regarding the business, wouldn't it be more appropriate to categorise the members' interests in the same group with the company's interests, than with the employees? What in fact are the interests of its members?

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[167] Refer to s. 39. Unlike in the case of a company limited by guarantee, the Act does not specify the type of businesses a company not limited by guarantee may engage in. Thus, as long as a venture is lawful and not illegal, a company is generally entitled to pursue it.

[168] Refer above, **3.2.2**

[169] *Brady vs. Brady* (1987) 3 BCC, 535 at 552 (CA); *Gaiman vs. National Association for Mental Health* (1971) Ch. at 330.

Following s. 279(3), it can be argued that the interests of the members would most likely also be to preserve the company's assets, further its business and promote the purposes for which the company was formed which, ultimately, will result in favourable returns. On the other hand, the interests of employees would most certainly be towards keeping their jobs, promotion opportunities and earning better pay. Evidently, therefore, the two groups have diverse interests. Furthermore, any rights the employees may have are limited to their contracts of employment with the company and generally any labour rights recognised by statute,[170] as opposed to the bundle of ownership rights available to members under company law, including the right to attend and vote at meetings resolving to appoint or remove directors and generally deciding the future of the company. It is also significant that, unlike members/shareholders who have the medium of derivative actions through which to enforce the duties of directors albeit indirectly, the company's employees have no such means under company law. Conclusively, it is submitted that the director's duty to act in the best interests of the company in s. 279(3) cannot be practically isolated from his duty to have regard to the interests of its members in s. 279(4). Thus, the interests of members should have been aligned with those of the company, rather than the employees.

The matters to which the director is to have regard are presumably not limited to the two groups mentioned in s. 279(4). In line with the general rule of interpretation, the drafters' use of the word "includes" suggests that the director may have regard to other matters in the performance of his functions. Since the Act does not give any clue as to what those other matters may be, it would be safe to assume that so long as the director's regard of a particular factor does not cause him to act ultra vires the company's powers or its purpose, or contrary to its best interests, his action would be in order. Accordingly,

[170] The CAMA has also considered the company's employees in other respects. See ss. 342(5), 384 and 566.

the director may, under appropriate circumstances, consider the interests of outsiders such as the company's consumers, suppliers or host community, for example, if this would ultimately be in the best interests of the company.

Curiously, s. 279(5) cautions that "a director shall exercise his powers for the purpose for which *he* is specified and shall not do so for a collateral purpose, and the power, if exercised for the right purposes does not constitute a breach of duty, if it incidentally affects a member adversely." It is not clear from the subsection what is meant by "his powers", especially since the subsection continues with "for which *he* is specified". The word, "specified" suggests that the powers referred to are clearly stated somewhere. But it is not clear from this particular provision, what those powers are or where they are likely to be found.[171]

However, s.63(2) provides inter alia, that "the...powers of...the board of directors shall be determined by the company's articles." But these powers belong to the collective board not to individual directors. The articles of association prescribe regulations for the management of the company[172] and when registered along with the memorandum, shall have the effect of a contract under seal between the company and its members and officers, and between the members and officers themselves, whereby they agree to observe and perform the provisions therein.[173]Thus, any "powers" a director may have would more likely be *specified*, or better still, *conferred* on him, by the articles of association, by which he is guided in his actions. If this subsection is to be reconstructed to make proper sense, therefore, it should at least make proper reference to the source of the *powers*, so that a director may be better guided in his duty. A reconstruction may read: "a director shall act in accordance with *powers* conferred by

[171]S.263(5) also states that "directors may delegate their powers…." Still, the provision does not point out the likely source of those "powers."
[172] Refer to s. 33.
[173] Refer to s. 41(1)

the company's articles or this Act, for the purposes for which *they areconferred* and not for a collateral purpose...." This way, the meaning of the *purpose* here would follow from s. 279(3) where it was previously stated as ultimately, *the purpose for which the company was formed*. This interpretation would also be in line with s. 38, which states that "every company shall, for the furtherance of its authorised business or objects, have all the powers of a natural person of full capacity," and which powers, presumably, would be exercised in accordance with its articles.

The *powers* referred to mustflow directly from those conferred on every company by the CAMA by virtue of registration under the law, which powers are solely for the promotion, furtherance or achievement of its business or object and which its articles in turn endorse to be exercised by its directors.[174] If the concept of the company is understood as an individual which, though having legal personality, is artificial and therefore, has no organs of its own to carry out acts and that the directors are thereby its mind and limbs as well as its agents, it therefore follows that whatever "powers" they wield are not in fact theirs but the company's, and for it.[175]

"Collateral purpose" suggests any purpose which is not among those specified, or purpose which cannot be interpreted as being the purpose for which the company was formed.[176] It can also be interpreted by contrasting the director's duty to act bona fide in the interest of the company[177] and his duty to avoid what the Act terms "conflict of duties and interests."[178]

Judicial decisions reached on the point of the subsections under consideration considerably aid in understanding the intendment of the legislature, however

[174] See ss. 37, 38(1) and 63(2).
[175] See s. 63(3). When the directors act collectively as a board, the modern view is not so much that they are agents of the company but that, so long as they act within their powers, they act as *thecompany*. See Davies, L.P. and Worthington, S. op.cit. at 526.
[176] Refer to s.279(3).
[177] Refer to s.279(1).
[178] Refer to ss. 280 and 281. To be discussed later in this work.

unsuccessful the latter may have been in the choice of proper diction in capturing the law. Now, relevant cases are considered in turn.

S. 279(3) and (5) may have been enacted with **Re Smith & Fawcett Ltd.**[179] in mind because of the similar wordings used. Therein, Lord Greene M.R. remarked that directors were required to act "bona fide in what they consider—not what a court may consider—is in the interests of the company...and not for any collateral purpose".[180] By this interpretation, the section suggests a subjective test for the directors and accordingly, the court intends that directors should retain the ultimate decision as to what course of action is right for their company in a business sense. A fortiori, the court will not take it upon itself to order that a particular power vested in directors should be exercised in a particular way.[181] In the words of Lord Wilberforce,

> *It would be wrong for the court to substitute its opinion for that of the management, or indeed to question the correctness of the management's decision...if bona fide arrived at. There is no appeal on merits from management decisions to courts of law: nor will courts of law assume to act as a kind of supervisory board over decisions within the powers of management honestly arrived at.*[182]

Conclusively, therefore, any power conferred on directors, whether by the articles or any contract, is part of their management power. This is so even where the power is discretionary. In **Artra Industries Nig. Ltd. vs. Nigerian Bank for Commerce and Industry**,[183] the plaintiff had obtained a secured loan from the defendant. A clause in the loan agreement conferred "discretionary power" on the defendant to decide whether or not to grant the plaintiff consent to further mortgage or charge the security with a third party. When the plaintiff sought this consent the first time, the defendant granted it. But

[179](1942) Ch. 304 CA.
[180]Ibid., at 306.
[181]*Pergamon Press Ltd. vs. Maxwell* (1970) 1 WLR 1167.
[182]*Howard Smith Ltd. vs. Ampol Petroleum Ltd*. (1974) A.C. 821, at 834.
[183](1998) 3 SCNJ, 97.

when it further sought to create a third charge on the same security, the defendant declined to consent. The plaintiff then sued for, among others, damages suffered by it as a result of the defendant's refusal to grant consent for the further charge, which would have enabled it to obtain a working capital for its venture. Citing s. 279(3), the apex court concluded:

> *There is no doubt that the exercise of discretionary power, such as in this case, falls within the management power which is, by section 63(3), conferred on directors. In exercise of such power, the directors must adhere strictly to the statutory provision which enjoins them to consider the interest of the company as paramount...The directors of the defendant bank being therefore alert to their responsibilities, could not have exercised their discretion in favour of the plaintiff, the proper effect of which would be to further dilute the defendant's security, when the plaintiff was already in breach of its previous undertaking.*[184]

Similarly, Coker J.S.C. observed in **Adebayo vs. Johnson**,[185] that

> *The authorities establish clearly that…the courts have consistently adopted the view that they would not, as Parliament has thought it fit not to, embarrass or unsettle business-men in the performance of their vocations. Those who organise, manage or control trade or business or both are generally entitled to depend upon their own ability, prudence and judgment.*[186]

The foregoing notwithstanding, cases have often been brought before the court asking it to determine whether or not directors have not in fact acted in bad faith and contrary to the best interests of the company, but in their own interests. In determining liability in any given case, the court asks itself whether it has been proved that the directors had not done what they believed to be right.[187] In other words, the burden of proof is on those who assert that they have not. In the case of **Re Smith & Fawcett**

[184]Per Onu, J.S.C. at 124.
[185](1969) All NLR, 171.
[186]Ibid., at 180.
[187]Davies, L.P. and Worthington, S. op.cit.at545.

Ltd.,[188] for instance, where a clause in the articles regarding the admission of new members into the private company conferred on the directors a discretion with regard to the acceptance of transfer of shares, the directors refused to register transfer in a particular case, but agreed that they would register a transfer of part of the shareholding, if the transferor agreed to sell the balance to one of the directors at a stated price. The court considered this decision of the directors as insufficient evidence of bad faith and confirmed the directors' discretion to exercise their judgment.

Thus, proving the directors' bad faith is no easy task. The court would normally accept that the directors had acted in good faith, unless satisfied that they had not behaved as honest men of business might be expected to act. However, because of the subjective nature of the provision, even where a director had not acted as expected of an honest business person, this would not necessarily be considered a demonstration of a breach of the duty to act in good faith.[189] In **Regentcrest Plc. (in liquidation) vs. Cohen**,[190] where the directors' decision had caused substantial harm to the company, it was held that this was, at most, merely a strong piece of evidence against their contention that they had acted in good faith, rather than absolute proof that they had not.

As trustees are required to act bona fide in the best interests of their beneficiaries, so are directors required to act in the best interests of the company. The question is: what in fact, are "the best interests of the company"? The decisions above suggest that there is a link between the director's good faith judgment and the company's best interests because, ultimately, he decides what they are. This essentially endows the director with immense powers. While s. 279(3) gives the director pointers that the best interests of the company would be towards preserving its assets, furthering its business and promoting the purposes for which it was formed, s. 279(5) further warns

[188]Supra.
[189]Davies, L.P. and Worthington, S. op.cit.at 545.
[190](2001) 2 B.C.L. 80 Ch. D.

him against not exercising his power for the purpose conferred but for a collateral purpose. Collateral purpose would most likely be either to feather the director's own nest, or to preserve his control of the company in his own interests,[191] thereby acting *malafide* and causing a conflict between his duties to the company and his personal interests.

It is more often in the illegitimate use of legitimate powers, that directors are found wanting on this point. Prima facie, powers conferred on directors by the articles of association of companies must be used bona fide for the benefit of the company as a whole, otherwise, improper use may even amount to fraud.[192] It has been suggested that, in any transaction, the proper test is "whether an intelligent and honest man in the position of the director concerned could, in the circumstances have reasonably believed that the transaction was for the benefit of the company."[193] In **Rolled Steel Products (Holdings) Ltd vs. British Steel Corporation**,[194] a Mr Shenkman was a majority shareholder and one of two directors in Rolled Steel and also held all the issued share capital in Scottish Steel of which he was also a director. The latter company owed a lot of money to BSC, which loan Shenkaman personally guaranteed. When BSC wanted more security, Shenkman caused Rolled Steel to enter into a guarantee of the debt, without any benefit whatsoever to Rolled Steel.

The Court of Appeal decided that although the transaction was not *ultravires* Rolled Steel since its objects clause granted express powers for the company to enter into guarantees, still Mr Shenkman and the other director—his father—had exercised their powers of giving the guarantee for an improper purpose, knowing full well that

[191]Davies, L.P. and Worthington, S. op.cit.at 528.
[192]See *Ngurli Ltd. vs. McCann* (1953) 90 CLR 425 at 438, where it was decided that it was a fraud for the controlling director to abuse the power to issue shares conferred on him by the articles.
[193]*Charterbridge Corporation Ltd. vs. Lloyds Bank* (1970) Ch 62.
[194](1985) 2 WLR 908.

there was no benefit to Rolled Steel in the guarantee. Accordingly, the guarantee could be avoided.

In **Re W & M Roith Ltd.**, the controlling director wished to make provision for his widow. Consequently, he entered into a service agreement with the company whereby on his death, she was entitled to a pension for life. On being satisfied that no thought had been given to the question whether the arrangement was for the benefit of the company and that, indeed, the sole object was to make provision for the widow, the court held that the transaction was not binding on the company. The directors were unable to prove the corporate benefit of the transaction.

Perhaps in no more situations is the directors' motive questioned than in matters of share allotment. Being a fiduciary power, share allotment prerogative must be exercised bona fide in what the directors consider to be in the interests of the company and not for some collateral purpose.[195] They would not, for example, be allowed to issue shares to their nominees in order to retain control of the company. Many decisions regarding directors' resort to the use of the so-called poison pill device[196] also reiterate this.

In **Hogg vs. Cramphorn Ltd.**,[197] Buckley J held that an allotment of shares (each with weighted voting power) made bona fide by the board, but with the intention of defeating a possible takeover bid and of retaining the present board in control, was an improper exercise of that power. The fact that the directors undoubtedly "acted throughout in the belief that what they were doing was for the good of the

[195] Per Meggary VC in *Cayne vs. Global Natural Resources Plc*. (unreported) Chancery Division of the High Court of Justice, 12th August, 1982, cited in Corkery, F.J. op.cit. at110.
[196] North American jargon for a legal device of any form put in place by the management of a company that feels vulnerable to predatory or hostile acquisition, designed as a defence mechanism to eliminate or reduce that risk. Other expressions such as "shark repellent" are also used. See Wild, C. and Weinstein, S.op.cit.at 337.
[197](1967) Ch. 254.

company"[198]was of no avail. The complaint of the minority shareholder, Mr Baxter, was accepted. The issue was shown to be "intended not only to ensure that, if Mr Baxter succeeded in obtaining a shareholding which, as matters stood, would have been a controlling shareholding, he should not secure control of the company, but also, and perhaps primarily, to discourage Mr Baxter from proceeding with his bid at all".[199]

In **Howard Smith Ltd. vs. Ampol Petroleum Ltd.**,[200]Ampol, which together with an associated company, was a majority shareholder in a company called Millers, made an offer to acquire the rest of the shares in Millers. But the directors of Millers preferred another takeover offer from Howard Smith, whose terms the directors considered better, since it offered them employment in the future. Unfortunately, the latter's bid could not succeed as long as Ampol regained its majority holding. Consequently, the directors of Millers caused the company to issue sufficient new shares to Howard Smith, so that Ampol was as a result reduced to a minority position and Howard Smith could then more successfully launch its offer, since its bid price was higher than Ampol's offer. Under the articles of Millers, the directors had power to allot unissued shares to such persons and on such terms as they thought fit.

In proceedings brought by Ampol against, inter alia, the directors and Howard Smith, it was argued that the only proper purpose for which a share-issue power could be exercised was to raise new capital when the company needed it. But this was rejected as too narrow.[201] There might be a range of purposes for which a company may issue shares. The directors had maintained that the new shares were necessary because the company required capital to purchase two new tankers and this they cited as the dominant purpose for the issue of the new shares. But Street J. at the lower New South

[198]Ibid., at 262.
[199]Per Buckley J. ibid. at 265-266. The earlier decision of *Punt vs. Symons & Co. Ltd*. (1903) 2 Ch. 506 was similarly decided.
[200](1974) A.C. 821.
[201]Supra at 835-836.

Wales Supreme Court, found this argument "unreal and unconvincing". If there happen to be potentially many purposes for the directors' action in any given case, the court would consider the dominant or primary purpose which the directors had.[202]

In giving the judgment of the Privy Council, Lord Wilberforce stated that a decision of directors to issue shares could be set aside on the ground of improper purpose even though there was no element of self-interest involved, and that while it might in some circumstances be proper to issue shares for purposes other than raising capital for the company, "it must be unconstitutional for directors to use their fiduciary powers over the shares in the company purely for the purpose of destroying an existing majority, or creating a new majority which did not previously exist." Further, he observed that the case was all the stronger against the directors where there was "an ulterior purpose to enable an offer for shares to proceed which the existing majority was in a position to block."[203] Thus, where the self-interest of the directors is involved, the court would generally reject any plea that their action was bona fide in the interest of the company, just as it would reject the plea of a trustee that he paid a good price, if he bought trust property.[204] Accordingly, the Privy Council held that the board of Millers had acted with an *improperpurpose*, albeit honestly and within their powers, and that the issue of shares to the bidder should thus be set aside.

In spite of the presumably strict rules set by the foregoing cases, some decisions coming later considered the possibility that under certain circumstances, the court may uphold the directors issuing powers if commercially justified in the corporate interest and regardless of the fact that it incidentally results in putting off a takeover.[205] In

[202]Davies, L.P. and Worthington, S.op.cit.at 530.
[203]Supra at 837.
[204]Supra at 834.
[205]*Pine Vale Investments Ltd. vs. McDonnell and East Ltd.* (1983) 1 A.C.L.C. 1294 at 1304. Earlier decisions, including *Harlowe's Nominees Pty Ltd. vs. Woodside (Lakes Engrance) Oil Co. NL* (1968) 121

Cayne vs. Global Natural Resources Plc.,[206]Megarry VC warned that the principle in **Hogg** must not be carried too far, particularly in instances where a competitor aims to take over in order to annihilate the target company. It would be a perfectly proper exercise of the fiduciary powers of the directors of the latter to issue shares to defeat their competitor's purpose, if the only means available to the directors for achieving that was to retain control.[207] The more recent decision of the English court in **Criterion Properties Plc. vs. Stratford UK Properties LLC**,[208] also considered it possible that in some cases, it might be a proper purpose of the exercise of directors' powers to block or discourage a takeover.

Depending on the circumstances, there are a multitude of purposes for which directors can properly issue shares, including the fostering of desirable business connections,[209] the maintenance of the minimum necessary membership in the company[210] and improvement of the company's financial position.[211] The courts have equally decided many improper or collateral purposes for which directors have issued shares, including the defeat of a takeover, the entrenchment of a board in control of a company, benefiting some shareholders or their friends at the expense of other shareholders or so that some shareholders or their friends could wrest control from the other shareholders,[212] and the prevention of interests unfriendly to the directors from gaining power.[213]

CLR 483 and *Teck Corporation Ltd. vs. Millar* (1973) 33 DLR (3d) 288 Sup. Ct. (BC) also supported this position.

[206] (unreported) Chancery Division of the High Court of Justice, 12th August, 1982, cited in Corkery, F.J. op.cit. at 110.

[207] Appeal over the refusal to issue injunctions for the directors' action dismissed: (1984) 1 All ER 225.

[208](2002) 2 BCLC 151.

[209]*Harlowe's Nominees Pty Ltd. vs. Woodside (Lakes Engrance) Oil Co. NL* (1968) 121 CLR 483.

[210]*Punt vs. Symons* (1903) 2 Ch. 506 at 516.

[211]*Winthrop Investments Ltd. vs. Winns Ltd*. (1975) 2 N.S.W.L.R. 666, NSWCA.

[212]*Ngurli Ltd. vs. McCann* (1953) 90 CLR 425 at 440.

[213]Franzi, N.C.A. (1976).The Subjective and Objective Elements of a Company Boards' Power to Issue Shares.*Melbourne University Law Review*, 10(3): 392 at p.395.

Where there appears to be a multiplicity of purposes for which the directors might have acted—as was the case in **Ampol** above—the test of illegality must be applied to the dominant or primary purpose which the directors had and which the court must first identify. If, as is most likely, it is the articles that confer the powers in question on the directors, it has been posited that "...it is for the court to decide on a true interpretation of the articles what the purpose was for which the power was conferred."[214]

Prentice observed that the proper purpose doctrine has no independent existence outside the articles of association and that appropriately drafted articles can determine which purposes are proper and which are improper.[215] Indeed, there appears to be some credence to this opinion. S. 124 reserves the power of allotment of shares in the company. However, the same section allows the company to delegate this power to its directors, and the articles to state how this power is to be exercised. Thus, in order to allow directors to be able to, for instance, stave off a takeover bid or prevent a new control over the company, the articles of association can be appropriately drafted to have the required effect. The courts, in any given case, would normally simply give the articles the interpretation intended by their drafters, so long as it is not contrary to law, and so long as the directors acted in good faith and thought they were acting in the best interests of the company at the material time. A fortiori, the court would not venture to interfere with the directors' bona fide exercise of their powers for the right purposes simply because it incidentally affects a member adversely.[216]

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[214] Ali, H.L. *op.cit.,*fn 50 at 162, citing Gower, L.C.B. *Company Directors and Controllers,* Australia, p. 64. See also *Re Smith & Fawcett Ltd.* (1942) Ch. 304 at 306.

[215]Prentice, D.D. (1970).Expulsion of Members from a Company. *The Modern Law Review*, 33: 700-704, at 703.

[216] See s. 279(5) and the decision in *Mills vs. Mills* (1938) 60 CLR 150, where it was decided that where the directors' decision would benefit some but adversely affect other members, they should simply consider what is fair between the two.

While s. 279(4) allows directors to consider the interests of the company's employees, that consideration is subject to the overriding duty of acting in the best interests of the company. S. 342(5) also suggests that the company may invest in the health, safety and welfare of its employees, which, while being in the latter's interest, would obviously be to the company's ultimate benefit. So would any agreement reached on employee incentives in the form of sharing in corporate profits.[217] Thus, where directors' claim to be acting in the interest of the company, they must also show that their action is in fact for its benefit.

But the interest of employees has not always been within the contemplation of company law. Back in 1883, Bowen L.J. famously maintained, regarding gratuitous grants to employees, that

> *As soon as a question is raised by a dissentient shareholder…sympathy must be cut adrift, and we have to consider what the law is…[Directors] can only spend money which is not theirs but the company's, if they are spending it for purposes that are reasonably incidental to carrying on the business of the company. That is the general doctrine. Bona fides cannot be the sole test, otherwise you might have a lunatic conducting the affairs of the company and paying away its money with both hands in a manner perfectly bona fide yet perfectly irrational…it is for the directors to judge, provided it is a matter which is reasonably incidental to the carrying on of the business of the company… The law does not say that there are to be no cakes and ale, but there are to be no cakes and ale except such as are required for the benefit of the company. Charity has no business to sit at Boards of directors qua charity. There is however a kind of charitable dealing which is for the interest of those who practice it, and to that extent…charity may sit at the Board, but for no other purpose.*[218]

[217] And this, whether or not dividends have been declared. See s. 384.

[218] *Hutton vs. West Cork Railway* (1883) 23 Ch. D. 654 at 673. A similar decision was reached almost a century later in *Re W & M Roith Ltd.* (1967) 1 W.L.R. 432, where the court refused to allow an agreement between the company and its director, in which the company agreed to provide his widow with a pension for life.

The dictum above reiterates that directors are first and foremost trustees: they cannot pay away monies other than for the benefit of their *cestuique trust*, in this case, the company, however noble the intention. Similarly, in **Parke vs. Daily News Ltd.**,[219] the defendant company sold the major part of its business and proposed to use the proceeds to make payments to employees by way of redundancy pay. The court held that such payments were not for the benefit of the company, but rather for the benefit of the employees and, therefore, the company had no power to make the payments. In other words, the payment failed because it could not be argued that a company about to enter liquidation any longer had any interest in fostering good relations with its employees.[220]

The provisions in ss. 518 and 566 clearly reject the decision in **Parke**above. Consequently, a company may make provision for employees or former employees in connection with the cessation or transfer of the undertaking of the company or its subsidiary, notwithstanding that this is not in the best interest of the company. However, it is clear from the tenor of the law that it is merely discretionary for the company to so provide for its employees. In the absence of an independent enforceable agreement between the company and the employees to that effect, it is highly unlikely that the latter can enforce this provision against the company.

The case of **Virgin Tech. Ltd. vs. Mohammed and Bank PHB**[221] was an apt example of a clear breach of the duty under s.279(3). Unfortunately, the action was not instituted on that section. The respondent in that case, who also happened to be a director and co-signatory to the appellant's account, caused the transfer of the sum of N199,660,000.00 from the latter's account to her personal account with the second respondent. When attempts at persuading her to return the money failed, the CEO then

[219](1962) Ch. 927.
[220] Also see the decisions in *Dodge vs. Ford Motor Co*. supra
[221](2009) 11 NWLR (Pt. 1151) 136 C.A.

instituted an action in the name of the company against the respondents. The court granted judgment for the appellant.

Generally, the same observation noted regarding scarcity of local decisions on the duty of care and skill, apply here. Again, government agencies more often left to take charge of cases of erring directors in the area of fiduciary duties, particularly in cases involving financial institutions. A classic example is the case of former Intercontinental BankPlc, where the Economic and Financial Crimes Commission (EFCC) filed fraud related charges against seven of the directors for, inter alia, granting over 60 billion naira loans to companies in which they allegedly had interests, without adequate collateral.[222] This is quite easily a matter of breach of the duties to act in good faith and in the best interests of the company. A similar case is that involving Cecilia Ibru of former Oceanic Bank Plc. who was sentenced in October 2010 and ordered to handover $1.2 billion in cash and assets, as well as serve 6 months' jail term.[223] The Cadbury case mentioned earlier might also have been a case of a breach of fiduciary duties, for the directors did not act in good faith, in the best interests of the company in using the company's money to continuously produce products that were not selling and even borrowing in order to do that.[224] The sanction of simply dismissing the directors without more, it has been suggested, fell short of expectation.[225] It is regretful that the erring directors above were not tried under the appropriate sections on directors' duties so that we might have a rich case law in that area.

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[222] See Anaba, I. and Adeshida, A. (2009). EFCC Files Charges AgainstIbru, Ebong, Thirteen Others. *Vanguard.*Retrieved May 2, 2014, from http://www.vanguardngr.com/2009/08/efcc-files-charges-against-ibru-ebong-13-others/

[223] See BBC News Africa. Retrieved May 5, 2014, from http://www.bbc.co.uk/news/world-africa-11506421.

[224] It was alleged that under the MD's watch, the company went as far as procuring loans for its customers so as to enable them pay for the products they were not at the time prepared to take, in order that the balance sheet of the company may reflect that the goods had been paid for.

[225] See Why Bunmi Oni, Auditor, Must be Prosecuted. *Proshare*.Retrieved May 5, 2014, from http://www.proshareng.com/articles/847/Why-Bunmi-Oni-Auditor-Must-Be-Prosecuted.

3.6 Duty Not to Fetter Discretion to Vote

This duty seeks to ensure the director's loyalty to the main objective of acting in the best interests of the company, which is paramount. The director is bound by the company's articles, which state his powers, how they are to be exercised as well as their limits. Thus, when he votes at resolutions, he is only bound by his fiduciary duty to the company and nothing else. Any collateral agreement with any person aiming to restrict the way the director votes at resolutions would be unlawful. The modern phenomena of the requirement for independent nonexecutive directors on the ideal board[226] may have been intended to reinforce this rule.

S. 279(6) is emphatic that "a director shall not fetter his discretion to vote in a particular way." In ordinary parlance, to "fetter" means to restrict, restrain or limit;[227] to restrict someone's freedom and prevent them from doing what they want.[228] By the provision above, even though the CAMA only specifies the director's "vote", it is generally intended that the director should maintain his independent judgment at all times.

S. 279(6) however, fails to specify what circumstances may amount to fettering the director's discretion or how this may come about. A clue can be found in s. 279(5) which warns that the director must not exercise his powers for a collateral purpose. The director agreeing to restrict the manner in which he votes can result in using his voting powers for a collateral purpose as opposed to the proper purpose which should be *at all times what he believes to be the best interests of the company.* He must not favour any sectional interests, either.[229] In the case of **Clark vs. Workman**[230] regarding the refusal

[226] Refer to paragraph 5.5.(c) of the SEC Code of Corporate Governance for Public Companies 2011 and 5.3.6 of the CBN Code of Corporate Governance for Banks Post Consolidation 2006.
[227] Encarta Dictionaries (2009).Microsoft Encarta Premium DVD.
[228] Longman Dictionary of Contemporary English, op.cit.at585.
[229] See s.283(1).
[230] (1920) 1 Ir. R. 107.

by the directors of a company to register transfer of shares, evidence that the directors were acting upon undertakings given to outsiders was considered evidence that their discretion was being improperly exercised. The court reiterated that the directors of a company must act strictly as trustees in carrying through transfers of shares, unfettered by any undertaking or promise to any intending purchaser.

Another possible circumstance that may cause a call upon the director not to fetter his discretion to vote may occur in instances where he happens to be a multiple director,[231] especially of competing companies. In this case, it has been observed that one who is a director of two rival concerns is walking a tight-rope and at risk if he fails to deal fairly with both.[232] The same applies to a representative/nominee director of a member company who sits at the board by virtue of the membership of another company in the company of which he is a director.[233]This director may not also agree with the company he is representing, to terms fettering his discretion to vote.[234] Where the articles allow a director to appoint a nominee, a nominee so appointed would not be found to have fettered his discretion unless it is found that he put the interests of his appointer above those of the company.[235]

It is significant that s. 279(8) does not allow any derogation from this rule by means of the company's articles, resolutions or through the terms of any contract. Clearly, the law intends that the director should not easily wriggle out of this obligation, even with the consent of the company. However, in modern times, this may not be good for business in certain situations. If the law forbids the directors, *collectively* acting in

[231] The CAMA allows this by implication. See s. 281.
[232] Per Lord Denning in *Scottish Co-operative Wholesale Society Ltd. vs. Meyer* (1959) A.C., 324 HL at 366-368
[233]S.257(1)(d) forbids corporate directorship, but allows the representative of another company to be appointed to the board for a given term.
[234] See *Selangor United Rubber Estates Ltd. vs. Craddock* (1968) 2 All ER 1073.
[235]*Scottish Co-operative Wholesale Society Ltd. vs. Meyer* (1959) A.C., 324 HL; *Re Neath Rugby Ltd.* (2008) 1 BCLC 868 (PC)

the name of the company, from contracting with third parties to ensure that the company acts in a certain way in the future for the furtherance of the company's relations with its business partners or fulfilling the terms of its contracts, this may fetter the company's prospects.

It is argued that if individuals may contract as to their future behaviour in business matters, it is desirable that companies, through their directors, should be able to do so too, for, deciding otherwise has the potential to make companies unreliable contracting parties or of depriving them of opportunities to enter into long-term contracts which would be to their benefit.[236] This may be the case, for example, where a company's prospective creditor requires a resolution of the company's board of directors to desist from causing the company to incur future debt liabilities, until the proposed loan is repaid, before he/it would agree to give the loan.

3.7 Duty not to Allow Duty to Conflict with Personal Interest

The director of a company, being a fiduciary, is bound by the usual rules applying to fiduciaries generally, including the rule against using the opportunities gained by virtue of the office he holds, for his personal benefit. He must thus avoid a situation whereby his fiduciary duty to the company conflicts with any personal interest. The idea is that he must not make any profit out of his position in the company beyond his agreed remuneration, without the consent of the company.[237] The director's duty here broadly encompasses situations where he misuses the company's information or property; enters into contracts with the company; or receives any benefit from third parties by virtue of his office. The latter aspect will be the proper subject of the next sub-heading in this work. The first two will form the subject under discussion here. The principles are partly codified in s. 280 thus:

[236] Davies, L.P. and Worthington, S.op.cit.at 538.
[237] *Boston Deep Sea Fishing and Ice Co. vs. Ansell* (1888) 39 Ch. D. 339 (CA).

> *(1) The personal interest of a director shall not conflict with any of his duties as a director under this Act*
> *(2) A director shall not*
> *(a) in the course of management of affairs of the company; or*
> *(b) in the utilisation of the company's property, make any secret profit or achieve other unnecessary benefits.*
> *(3) A director shall be accountable to the company for any secret profit made by him or any unnecessary benefit derived by him contrary to the provisions of subsection (2) of this section.*
> *(4) The inability or unwillingness of the company to perform any functions or duties under its articles and memorandum shall not constitute a defence to any breach of duty of a director under this Act.*
> *(5) the duty not to misuse corporate information shall not cease by a director or an officer having resigned from the company and he shall be accountable and can be restrained by an injunction from misusing the information received by virtue of his previous position.*
> *(6) where a director discloses his interests before the transaction and before the secret profits are made before the general meeting, which may or may not authorise any resulting profits, he may escape liability, but he shall not escape liability if he discloses only after he has made the secret profits, and in this case, he shall account for the profits.*

On a careful analysis of the above provisions, it can be discovered, firstly, that the diction used in subsection (1), in particular, "shall not" is rather inappropriate—considering the fact that the mind of the director is not something that can be controlled by the law—and amounts to a mere *positive statement* at best. A more appropriate choice of words could have been "must not" which is in the tone of an obligation and more emphatic; presumably what the law intends.[238]

Secondly, s.280(1) is couched in general terms and, without acknowledging exceptions, seems to neglect the fact that s.277 before it allows conflict of interest when the director contracts with the company. If the subsection had clearly identified the

[238] Refer to **1.1** supra on this note.

situations of conflict being addressed, it would not have appeared so contradictory in comparison with s.277.

Thirdly, and related to the point immediately preceding this, subsection (2) mentions "secret profit" and "unnecessary benefit". While the former may quite easily be understood, the latter, while being broad enough to admit a wide variety of situations, would appear rather vague to the average director. This becomes apparent especially when one considers that the common law equivalent of the duty covers corporate property, information and opportunity. It is submitted that if the law intends for wider interpretation as well as guidance, this can be achieved by complementing "unnecessary benefits" with "such as (or including) the exploitation (or misuse) of corporate information or opportunity". In this way, even the most unsophisticated director can have an idea of instances that might result in his breaching the law. Also, "unnecessary" may not quite be the appropriate qualifier for "benefit" as it would give room for a subjective judgment by the director. In other words, what makes a benefit *unnecessary*? It is submitted that "unauthorised" would be better suited here, especially considering subsection (6) allows authorisation.

Fourthly, and following the above, subsection (5) begins, "the duty not to misuse corporate information" and subsection (6) alludes to "the transaction". According to the rules of grammar, the use of the definite article "the" presupposes that the item has been mentioned or discussed before, or otherwise known to the reader. Here the subsections or previous sections have not previously mentioned "corporate information" or any "transaction." Their mention now would therefore seem belated. But if the suggestions

made as to improving subsection (2) above were to be adopted, this would take care of the perceived inconsistency.[239]

Finally, again following from the above, subsection (5) imposes a continuing duty only with respect to corporate information. Corporate property and opportunity have been neglected. It is submitted that the spirit of the law with regard to the prohibition of profits and conflicts contemplates profit in every form, whether information, property or opportunity.

Although the above rules are herein described as "duty" in this work as in many others, in the CAMA, their description as *principles* would be more apt because of the language in which they are stated,[240] though their application wouldin fact lead to duties imposed, such as duties of disclosure.[241] The principles are grounded in equity as is the nature of the director's position in the company. In the course of management, the director has the privilege of being privy to information regarding the company's operations, such as trade secrets, or prospective contracts or even having access to the company's property. He is more often involved in negotiating business transactions between his company and others. The law considers that under such circumstances, there is the danger of likely conflict between his fiduciary duty to the company and his personal interests. Thus, where a director, though himself not directly or indirectly involved in a contract with the company, has opportunity to benefit in any way during the course of managing the affairs of the company, it is the intendment of the law that he should enjoy no special benefits whether in the nature of opportunity, secret profit or use

[239] Alternatively, subsection (6) could, inter alia, read "where a director discloses his interests before any transaction that may cause a breach of duty not to misuse corporate information, property or opportunity, and before any secret profits are made..."

[240] Indeed, it has been suggested that to talk of directors' duties is a slight misnomer, as there are normally no positive duties on directors to act at all, but merely a prohibition on what they can do, should they decide to act. Thus the directors' duties are enforced negatively. See Prentice, D.D. (1967). Regal (Hastings) Ltd. vs. Gulliver: The Canadian Experience. The *Modern Law Review,* 30: 450 at p. 455.

[241] See Birds, J. et al.op.cit. note 111 atp. 645 on this note.

of information which otherwise he wouldn't have, if he were not that company's director. This is in fact directly linked to the fiduciary's duty to account.

Unarguably, the rule against making any personal gain in utilizing the company's property is straightforward. This is reinforced by the fact that s. 283(1) clearly makes the directors trustees of the company's monies and properties. There is thus obviously no room for personal gain where the company's properties are concerned.[242] The tricky part is when "unnecessary benefit" can be broadly interpreted to incorporate misuse of corporate opportunity and information. Most cases involve either or both of these two.

In **Nasr vs. Berini (Beirut-Riyadh) Bank (Nigeria) Ltd.**,[243] the plaintiff was a director to the defendant. Through an account opened in his nephew's name but in fact operated by him, he caused the defendant to advance money for the development of a property he owned. It was held that a director cannot cause the company to spend money on developing his own property without proper disclosure. The Supreme Court restated with approval the statement by the trial court that

> *It is a fundamental principle of company law that a director is precluded from dealing on behalf of the company with himself and from entering into engagements in which he has a personal interest conflicting or which possibly may conflict with the interest of those whom he is bound by fiduciary duty to protect...Any such dealing or engagement may however be affirmed or adopted by the company, provided such affirmation or adoption is not brought about by unfair or improper means.*[244]

Thus, the law recognises the right of the company to decide whether or not to let the director benefit from any transactions or use of corporate property. In line with s.280(6) the proper procedure is for the director to simply make a disclosure at the general meeting *before the transaction or secret profit is made* and the general meeting in turn

[242]Unless the company is privately owned by the same persons who happen to be its directors.
[243](1968) 1 All NLR, 274.
[244]Ibid., at 289.

would decide whether or not to authorise it. Otherwise, the company would be entitled to an account of any resulting profits.

A common law case often cited as a good illustration of the principles in s. 280 is **Industrial Development Consultants vs. Cooley**.[245] In that case, the defendant was the managing director of the plaintiff, which was a design and construction company. Being himself an architect of considerable distinction and attainment, he failed in an attempt to obtain for the plaintiff, a lucrative contract in regard to the building of four depots for a local gas board, which contract the plaintiff was very keen to obtain. The defendant was subsequently approached by the gas board with an offer to take up the contract in his private capacity, the gas board having made it clear to the defendant that it would not engage the plaintiff for the job, either way. He however concealed this offer from the plaintiff. Feigning illness, and because the board of the plaintiff was of the opinion that the defendant was near to a nervous breakdown, he was allowed to terminate his employment with them on short notice. Subsequently, the defendant took steps which resulted in his obtaining the contract for himself. The plaintiff thus sued him for an account of the profits he made on the contract.

In holding that the defendant had acted in breach of his duty to the plaintiff and must account, Roskill J. stated that the fact that the plaintiff might not have obtained the contract itself, was immaterial. "...there was always the possibility of the plaintiff persuading the gas board to change their minds and...it would have been the defendant's duty to try and persuade them to change their minds." The defendant was thus still liable to account to the company for the profit he made from the contract on the footing that he should have informed the company of the board's offer to him and that, after the offer was made, he "embarked on a deliberate policy and course of conduct which put his

[245](1972) 2 All ER 162.

personal interests as a potential contracting party with the gas board in direct conflict with his pre-existing and continuing duty as managing director of the plaintiff.[246]

This case illustrates two principles considered by the CAMA. First, the duty clearly survives the director's office so that he may not resign simply in order to avail himself of corporate opportunities.[247] Second, in such situations, it is no defence for the director to show that the company might not have made use of the information or opportunity.[248]

The application of the latter principle in **Regal (Hastings) Ltd. vs. Gulliver**[249] was considered by many to have gone too far. In that case, the appellant company owned one cinema in Hastings and wanted to buy two others with the intention of selling all three together. The Regal company then formed a subsidiary so that the subsidiary could buy the two cinemas in question. However, the landlord required a guarantee of the rent by the directors, unless the paid up capital of the subsidiary was £5,000. Since the directors were averse to providing a guarantee and the regal company could not provide £3,000 of the £5,000 required, the directors arranged it so that Regal company subscribed to 2000 shares and each of the five directors and Garton, the company's solicitor, took up 500 shares each. The subsidiary company then successfully acquired the two cinemas. Eventually, the transaction was not carried through by the sale of the property of the company as a going concern, but by the sale of all the shares in the appellant company and the subsidiary at a profit of almost £3 each. The new controllers of the Regal company then sued to recover the profit made by the directors and Garton.

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[246] Ibid. at 173-174.

[247] S.280(5). Prentice remarked, regarding the duty under consideration that "It would be fatuous to allow directors to immunise themselves against liability by resigning immediately prior to the acquisition of the opportunity." See Prentice, D.D. (1974). The Corporate Opportunity Doctrine. *The Modern Law Review,* 37: 464 at 467.

[248] See s. 280(4).

[249] (1942) 1 All ER 378.

Although it was found as a fact that all the transactions were bona fide, the House of Lords still held that the directors must account to the Regal Company for the profit on the grounds that it was only through the knowledge and opportunity they gained as its directors that they were able to obtain the shares and consequently, to make the profit. In particular, the court stated that the directors were liable to account to the company once it was established that (a) what the directors did was so related to the affairs of the company that it could properly be said to have been done in the course of their management and in utilisation of their opportunities and special knowledge as directors; and (b) what they did resulted in a profit to themselves. Their lordships also suggested that no question as to the right to retain this profit could have arisen if the directors had taken the precaution of obtaining the approval of the appellant company in general meeting, which would have been easy since they in fact controlled the voting.

As aforesaid, there have been criticisms regarding the decision above. The ruling suggested that the mere possession of information which results from the holding of office as a director is sufficient to raise the duty to account. Also, in this case, the directors already held majority of the shares, so that it would have been possible for them to obtain ratification of their acts by the company in general meeting anyway. Further, they had not really deprived the company of any of its property, since the shares in the subsidiary were bought with their own money and those shares had never in fact been the company's property.[250] Besides, the chairman was not ordered to account because he didn't take the 500 shares as beneficial owner, but caused two private companies of which he was a member and director, and his personal friend to take beneficially and not as his nominees. Likewise, the solicitor escaped because he took the shares at the express request of the board, even though the board had acted throughout

[250]Wild, C. and Weinstein, S.op.cit.at 335.

on his advice. Thus, the two men most responsible for what had been done escaped liability, while those who had followed their lead, paid up. And now, recovery by the company benefited only the purchasers, who only just came on the scene.[251] Consequently, it has been posited that this case has allowed "equitable principles" to be taken to "inequitable conclusions," especially because recovery was eventually not from the right people but in fact in favour of the wrong people.[252]

Regardless, it has equally been observed that the approach adopted by the courts may have been necessary as it effectually relieves the court of the difficult task of having to judge whether the company was genuinely unable to raise the finance itself, which judgment it is not well-placed to make. It is after all the duty of the director to obtain the opportunity for the company. One must agree with the position that if the director is to be relieved of this duty and left free to take the opportunity personally where there is only a low chance of the company obtaining the opportunity itself, this would give the director an incentive not to strive as hard as he ought to, in order to promote the company's interests.[253] Provisions such as s. 280(4) effectively remove this incentive. On the other hand, if the director makes a disclosure in accordance with s. 280(6), he would be allowed to take the advantage of any corporate opportunity or property, for the profit would then no longer be "secret". But he must account to the company in every other case.

Interestingly, perhaps in line with the principles of freedom of contract, the law does not forbid the director from holding multiple offices[254] even of rival companies,[255]

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[251]Davies, L.P. and Worthington, S. op.cit.at 593.
[252]Ibid. at 594.
[253] Davies, L.P. and Worthington, S. op.cit., p. 593. See also *Irving TrustCo.* vs. *Deutsche* (1934) 73 F. 2d 121, at 124 and*Industrial Development Consultants Ltd.* vs. *Cooley* (1972) 2 All E.R. 162at 176, where the court remarked, on the point under discussion, that"It is acurious position under which he whose duty it would have been to seek topersuade them to change their minds should now say that the plaintiffs sufferedno loss because he would never have succeeded in persuading them to change their mind."
[254] Refer to s. 281.

or setting up a rival business,[256] yet expects him to still discharge his fiduciary duties equally to each.[257] Thus, he must not use the property, opportunity or information obtained in the course of the management of one, for the benefit of the other, company or even his own or someone else's advantage.[258] However, the principles developed regarding the duties of the company director would make it very difficult for a person to successfully balance the interests of both businesses in such instances. Such a person is considered to be metaphorically walking a tight-rope and at risk if he fails to deal fairly with both.[259] On the other hand, nothing in the law prevents the company from drafting the director's terms of service in a way that prevents him from setting up a rival business or accepting a similar position in a rival company within the permissible boundaries of the general principles of contract regarding restrictive covenants.

Another limb of the principle against clash of interests and duty concerns situations where the director contracts with the company. The director is generally precluded from dealing on behalf of the company with himself—self-dealing—and from entering into engagements in which he has personal interests conflicting or which may possibly conflict with the interests of those whom he is bound by fiduciary duty to protect.[260] By virtue of his office, the director is an agent of the company and is said to be acting on its behalf. Where he contracts with the company in his personal capacity,

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[255] *London and Mashonaland Exploration Co. vs. New Mashonaland Exploration Co.* (1891) WN 165.Although the more modern approach is to restrict the holding of two offices unless the director has the consent of both companies.See Brown, E. (2010). A Case of Split Loyalty?Multiple Directorships and Conflicts of Interest under the Companies Act 2006.*Butterworths Journal of International Banking and Financial Law*, 584 at 585, citing *Bristol and West Building Society vs. Mothew*[1998] Ch 1 18, CA. Retrieved December 24, 2013, from http://www.essexcourt.net/uploads/publications/JIBFL_brown.pdf.

[256] *Bell vs. Lever Bros Ltd*. (1932) AC 161

[257] Refer to s. 281.

[258] Refer to s. 281. See *Bell vs. Lever Bros Ltd*. (1932) AC 161, where it was held that a director is not under an obligation to refrain from competing with his company or from becoming a director of a rival company, unless there is a contrary provision under the company's regulations for his contract of employment. See also *Scottish Co-operative Wholesale Society Ltd. vs. Meyer* (1958) 3 All ER 6.

[259] Per Lord Denning in *Scottish Co-operative Wholesale Society Ltd. vs. Meyer* (1959) A.C., 324 HL at 366-368.

[260] Per Sir Richard Baggalley in *Northwest Transportation Co. vs. Beatty* (1887) 12 APP, Cas 589, at 593.

while still being its director, there is a clash of interests. This principle of law is echoed in the statement of Lord Loughorough, that "he who undertakes to act for another in any matter, shall not in the same matter, act for himself."[261]

In order to guard against misuse of corporate opportunity and information, though the director is permitted to contract *with* the company whether directly or indirectly, he is severely restricted: s. 277 requires him to declare any interest he may have in a contract with the company, at a meeting of the board of directors, while s. 284 generally disqualifies him from buying from or selling to the company, any property with a value of not less than N2,000.00, unless the transaction is approved by the general meeting. Otherwise, the company can avoid the contract. Thus, in **Aberdeen Railway Co. vs. Blaikie**,[262] a contract between the company and a partnership of which one of the directors was a partner was avoided at the instance of the company, being a contract in which the director was *indirectly* interested. Profit made from the contract was equally recoverable.

It is conceded that placing a strict ban on the director's ability to contract with the company might not be in the interest of business. This is because in some cases, the director may be the best source of a particular asset required by the company and so, a ban on self-dealing will in fact be against the company's interests.[263] For instance, a director may happen to own a piece of land adjacent to the company's production premises, which land the company requires in order to expand its operations. Such situations inform the reason why the law allows the director to contract with the company, under certain circumstances. In any case, the law still expects him to observe

[261]*Whitecoat vs. Lawrence* (1798) Ves. 750. More to the point is the dictum of Lord Cairns in *Parker vs. McKenna* (1874) 10 Ch. App. 96, that "no man can in this court, acting as an agent, be allowed to put himself in a position in which his interest and duty will be in conflict."
[262](1854) 1 Macq 461, (1843-60) All ER Rep 249.
[263]Davies, L.P. and Worthington, S. op.cit.at 562.

the utmost good faith towards the company in any transaction with it.[264]It has been submitted earlier that, considering the frame of mind that constitutes "good faith" it would be almost impossible for a director to have that kind of attitude towards the company when he is transacting with it. Obviously, the law has been misstated here, especially considering the fact that the law effectively allows the director's personal interests to conflict with his duty, where he personally contracts with the company.[265]

S. 277 simply requiresthe director's disclosure, but mentions nothing about the company's approval. Presumably, the disclosure of the director's position would then allow the company make an informed decision whether or not to go ahead with the contract. It is disturbing that the law does not require the consideration of the transaction by the general meeting or at least, a disinterested board. The implication is that even the interested director or his cronies and other persons connected to him, can participate in the decision regarding the contract in question. This can allow the director take advantage of his position in the company.

It is as well that the section requires disclosure not only where the director has a direct interest, but equally where he has indirect interests. This would take care of situations where directors use their controlling shares in other companies, partnerships or family businesses to enter into such transactions. For instance, in **Transvaal Lands Co. vs. New Belgium (Transvaal) Land and Development Co.**,[266] a director of the plaintiff company, who was also a shareholder of the defendant company, voted in the meeting of the plaintiff's board for the purchase by the defendants, of the plaintiff's shares and without his vote, the contract would not have gone through. The court held that the transaction was void.

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[264]See s. 279(1); *Okeowo vs. Migliore* (1979) 11 SC, 113.

[265] See in particular ss.277 & 284 which allow the director to contract as an independent party, with the company.

[266](1914) 2 Ch. 488.

S.277 applies to both existing and proposed contracts, with criminal liability applying in both cases. This is as it should be because, in the case of proposed contracts, the thought of liability with a hefty fine would discourage the director from keeping his interests secret and in the case of existing contracts, the company may not readily have the civil remedies of rescission or avoidance available to it. And where the benefit derived by the director is so intertwined with those of a third party, getting him to account for the profits would be no easy task. However, the fine of N100 would hardly be considered punitive by reasonable standards today. There may be need for considerable review in this area.[267]

In the case of property transactions under s. 284, stricter regulations have been set. Apart from expressly including a shadow director, the rule extends to any person associated with the director, including members of his immediate family, as well as any company or trust associated with him. The approval of the general meeting is also required even after disclosure. Any such transaction entered into by the company in contravention of the provisions, is voidable at the instance of the company.[268] From the tenor of s. 284, even the articles cannot derogate from the rules set therein. It is submitted that similar rules should be adopted for s. 277 so that directors disclose to, and require the approval of, the general meeting,especially in the case of proposed contracts. Leaving it simply to the approval of the board may give the board an opportunity to ratify its own wrong-doing, especially where most or all of the directors stand to gain. This would be more likely where they are few.

There are other provisions discouraging directors from taking undue advantage of their position by conflictingtheir duty to the company with personal interest. These include s. 270 regarding prohibition of entry into guarantee or provision of security and

[267] Indeed, the same applies to all instances of fines imposed throughout the CAMA.
[268] See s. 286.

s. 273 which requires any payments made to a director by way of redundancy pay or retirement benefit to be disclosed to the general meeting for approval.

3.8 Duty Not to Accept Secret Benefits

A principle related to those mentioned in s. 280 above, is that which prohibits directors from accepting benefits of any kind from third parties in the course of discharging their duties to the company. S. 287(1) provides that "a director shall not accept a bribe, a gift, or commission either in cash or kind, from any person, or a share in the profit of that person in respect of any transaction involving his company *in order to introduce his company to deal with such a person*."

The director will still be in breach, even if he pleads that the company benefitted or that the gift was accepted in good faith,[269] and be liable to account to the company for what he got from the transaction,in addition to damages.[270]Since the law appears to disqualify the director's subjective judgment on the issue, so that his motive is not relevant, it is curious thatthe tenor of s.287(1) CAMA restricts the application of the rule to the motive of inducement. This is especially considering the fact that the idea behind the principle is to totally prohibit any unauthorised profits/gains by the director during the course of his duties. It is therefore submitted that the rule should apply even where there was no such inducement. The mere fact that the director received the gift or favour because of his office, should suffice.

The principle under discussion is aptly illustrated by the case of**Boston Deep Sea Fishing Co. vs. Ansell**.[271]There, a director of a fishing company contracted for the building of fishing vessels on its behalf. In the course of negotiations, he received a commission from the shipbuilders without disclosing this to the company. Although the

[269] Refer to s. 287(4).
[270] Refer to s. 287(2)
[271](1888) 39 Ch. D. 339, CA.

company had already dismissed him from office for some other misconduct before it found out about the secret commission, the court held him liable to account to the company for the commission he received.

Connected as this principle is to those mentioned in s. 280, it is curious that the provisions do not follow each other in the arrangement of sections in the CAMA, or better still, are not incorporated. A peripheral analysis of s. 287 would suggest that any situations falling under it are also adequately covered under s. 280. Yet, a more careful examination would reveal that s. 287 can be distinguished, firstly, to the extent that the director accepts the secret benefit specifically for one purpose: *in order to introduce*—or, more appropriately, induce—*his company to deal with any third parties*. Secondly, apart from accounting to the company, the director would also be liable for any damages sustained by the company. Finally and more importantly, while the situations covered by s. 280 can be authorised or approved by the general meeting, such is not the case with those of s. 287. This is because bribery isconsidered an offence generally so that there can be no room for its authorisation.

This principle especially resonates with Nigeria, being a country where anti-corruption is more often topmost on the reformation agenda of successive administrations. Corporate law is an ideal medium for combating corruption, particularly that involving bribery. This is because the institution of the company is ubiquitous amongst government and the general populace alike. In other words, those who control companies, more than any other persons, have more opportunities at discreet bribe profiteering, than most. In fact, good corporate governance has been identified as having

the potential to considerably weaken corrupt practices such as bribery, extortion and self-dealing.[272]

For the avoidance of doubt, the law goes as far as distinguishing bribery situations from those not so considered. Thus, the director is allowed to keep any gift—or better still, any benefit—if it was *unsolicited* and given as a sign of gratitude *after the transaction* that occasioned it was completed. Thus, for a gift to fall under this exception, these conditions must be satisfied cumulatively: the gift must first have been unsolicited for, offered as a sign of gratitude and offered after the transaction which occasioned it. However, the director must still declare it before the board and the fact recorded in the minutes' book for transparency.[273] It is unclear what would qualify a gift as *unsolicited*. This question is probably one for the courts, taking into consideration the circumstances of each case. Presumably, it would be for the director to prove that such was the case. But it is submitted that it would be easy for the director to arrange to receive the gift after the transaction and claim that the gift was unsolicited and, short of an outright confession from the giver, the company cannot be sure that this was in fact the case.

S. 287 clearly does not impose the duty on a former director. The disturbing conclusion is, where a director resigns, and then accepts a gift, benefit or commission which can reasonably be attributable to his former office, he cannot be liable under that section.

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[272]Hontz, E. and Shkolnikov, A.(Eds) (2009). *Corporate Governance: The Intersection of Public and Private Reforms.*Centre for International Private Enterprise, United States Agency for International Development, pp. 15, 27 and 31. Retrieved 27th September 2013, from www.cipe.org/sites/default/files/publication-docs/CG_USAID.pdf.It is also one of the principles of the United Nations Global Compact Ten Principles of Business that "businesses should work against corruption in all its forms, including extortion and bribery."Source: www.unglobalcompact.org/AboutTheGC/TheTenPrinciples/index.html.

[273] Refer to s. 287(3).

CHAPTER FOUR

DUTIES OF CARE AND SKILL AND FIDUCIARY DUTIES OF LOYALTY AND GOOD FAITH UNDER THE UK COMPANIES ACT

4.1 Introduction

Directors' duties under UK corporate law were hitherto not codified. Having been based in common law and equity, these principles have always provided the guidance for courts. But the enactment of the UK Companies Act 2006,[1] "the Act" brought many changes to the UK corporate scene, the most prominent of which was the codification of directors' duties for the first time. With the objective to improve corporate governance, this venture was intended to, as much as possible, standardize and consolidate the fragmented common law and equitable rulings related to the duties, as well as demystify that area for the average director, with the hope of eventually improving the level of compliance.

The Act, while substantially repealing the provisions of the UK Companies Act 1985, clearly preserves the pre-existing common law, but introduces a new dimension in the area of the company's relations with outsiders. The latter aspect of the new law is reported to have produced the most debate in parliament due to its novelty in corporate legislation.

While the Act contains both the general as well as specific statutory duties of directors, this work is predicated on the former, which every director owes individually. Any reference to sections herein shall be to the Act, unless otherwise stated. For clarity, "company", "firm" and "corporation" will be used interchangeably as having the same contextual meaning.

4.2 General Duties of Directors

[1] Unless otherwise stated, all sections cited in this chapter refer to this law.

The Act devotes the whole Chapter 2 of Part 10 to the general duties of directors.[2] They replace the common law rules in citation, though not necessarily in application and are by no means exhaustive of all the duties a director owes his company at any particular time. The duties still comprise the two categories of care and skill as well as loyalty and good faith. However, they are arranged in a more stylised manner within the Act, with aspects of overlapping duties addressed in separate sections, one after the other. The discussions under this chapter will follow a similar sequence.

As helpfully stated in the introductory section to the chapter on the duties, the general duties are based on certain common law rules and equitable principles and therefore, are meant to be interpreted and applied in much the same way.[3] Thus, the duties are applicable to every director, including a shadow director to the extent any common law rule or equitable principle would apply to him.[4]Accordingly, a shadow, unlike a de facto, director does not owe fiduciary duties.[5] However, a former director would still owe the duties to avoid conflict of interest and not to accept benefits from third parties.[6] The Act further acknowledges the general tendency of the duties to overlap, so that more than one of the general duties may apply to any given set of circumstances,[7] owing, in particular, to their common origins.

4.2.1 To Whom are the Duties Owed?

The introductory section to the chapter on directors' duties addresses the crucial preliminary question of to whom the duties therein are owed. Since duties by their

[2] See Appendix Aattached.
[3] Refer to s. 170(3) and (4). See also *Thermascan Ltd vs. Norman* [2009] EWHC 3694 (Ch). This statement may have been made in order to assuage the fears of critics who believed that the law, in codifying directors' duties, would tend to ossify and bring about inflexibility in this erstwhile versatile field.
[4] Refer to s. 170(5).
[5]*Ultraframe (UK) Ltd. vs. Fielding* (2005) EWHC 1638 (Ch); *Re Mea Corporation Ltd*. (2007) 1 BCLC 618.Although some other specific statutory duties under Chapters 3 and 4 of Part 10 to the Act, expressly apply to the shadow director. Refer generally to ss.187 and 223.
[6] Refer to s. 170(2)(a) and (b)
[7] Refer to s. 179.

nature require enforcement in order to be effective, it is important from the onset to discover to whom they are owed as the question of enforcement is very much dependent on it.

S. 170(1) states from the very beginning that "the general duties specified in ss. 171-177 are owed by a director of the company to the company." This point is especially significant for the duty to promote the success of the company expressed under s. 172. It is necessary for the law to make this statement because there are several interests where a company is concerned, the most influential of which are its members.[8] It is important that directors realise that although members have a stake and have certain exercisable rights in the affairs of the company, the directors' duty is still first and foremost to the corporation, which is in law a separate personality from any of its associates whatsoever.[9] The court's ruling in **Percival vs. Wright**[10] discussed previously[11] purported to set the record straight on the issue of any duties at all owed shareholders, albeit within certain limits. Thus, directors owe no duty to the company's members qua directors.

However, in clear agency situations, such as where shareholders authorise directors to sell their shares on their behalf, the courts recognise that the directors owe the shareholders a duty to account.[12] But the shareholders would then be vicariously liable in damages to any purchaser as principals, if the directors fraudulently misrepresent the state of the company's affairs to the purchaser.[13]

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[8] Stakeholder theorists often consider a long list of stakeholders having varying interests in the corporation. Refer to **3.4.2** supra on "In whose Interests and for whose Benefit should Directors Manage the Company?"

[9] Salomon vs. Salomon & Co. Ltd. (1897) A.C., 22; Macaura vs. Northern Assurance (1925) A.C. 619.

[10] (1902) 2 Ch. 421.

[11] Refer to **3.4.1**above on "Duties Owed to Whom?"

[12] *Allen vs. Hyatt* (1914) 30 T.L.R. 444 P.C.; *Briess vs. Wolley* (1954) 1 All E.R. 909.

[13] *Briess vs. Wolley* (1954) 1 All E.R. 909.

Court decisions have consistently shown that directors may owe fiduciary duties to shareholders under special circumstances. In **Coleman vs. Myers**,[14] for example, the Court of Appeal in New Zealand established that this is possible where a "special factual relationship" is established between the director(s) and shareholder(s) and especially where there is gross disparity of knowledge between the directors and the shareholders, so that the shareholders traditionally relied on the directors for information and advice.[15] This was certainly the case in **Platt vs. Platt**.[16] There, three brothers, C, D and K were shareholders in a BMW car dealership company. K ran the business and held ordinary shares, while C and D did not work in the business but held preference shares. The company did badly during the recession of the 1990s. Then, K was the only one in touch with BMW and the only director of the company. He misled his brothers by informing them that BMW was about to withdraw the franchise and was urging him to sell. Consequently, C and D transferred their preference shares to K for £1 each. These were said to be necessary to enable the business to be sold. Subsequently, profitable trading resumed and the business was not sold after all. Later, BMW did terminate the franchise and the business was sold leaving colossal profits. C and D who could not partake in them claimed damages for misrepresentation and breach of fiduciary duty by K.

The court accepted the proposition that a fiduciary duty existed in the circumstances, observing that, although the relationship between a company director and the shareholders of the company does not of itself give rise to fiduciary duties, special circumstances, as in the instant case, may require the imposition of such a duty. The latter decision was subsequently approved by the English Court of Appeal in

[14](1977) 2 N.Z.L.R. 225, N.Z.C.A.
[15] Refer to **3.4.1**supra on "Duties Owed to Whom?"
[16](1999) 2 B.C.L.C. 745.

Peskin vs. Anderson[17] though the court further reiterated that in the absence of such a special relationship, directors do not owe a duty to individual shareholders to keep them constantly informed of all matters that might affect their position even if the shareholders' decision on a sale of their shares would have been affected by that knowledge.

Where directors advice or inform the shareholders collectively on a takeover bid, the opinion of the courts is certainly different. The directors of the 'victim' company owe a duty to their shareholders *collectively* to be honest and not to mislead regarding the whole operation.[18] In **Re A Company**,[19] which was an allegation of unfair prejudice by some members of a private company against its directors regarding information on a takeover bid, Hoffmann J. decided that directors were not obliged to offer their shareholders advice on a takeover bid, although if they did, they must do so "with a view to enabling the shareholders...to sell, if they so wish, at the best price" and not for any ulterior purpose. This would place the directors in a fiduciary-like position as against the shareholders.[20]

Note that the cases above would more probably apply where private companies are involved as the 'target' or 'victim' of a takeover operation. In situations amounting to insider dealing[21] in public companies which are quoted on public securities markets—such as those operated by the London Stock Exchange, or PLUS Markets Plc.—the City Code on Takeovers and Mergers has stringent provisions enforceable against any director found to be in contravention of the rules therein pertaining to

[17] (2001) 1 B.C.L.C. 372
[18] *Gething vs. Kilner* (1972) 1 All ER, 1166.
[19] (1986) B.C.L.C. 382.
[20] Davies, L.P. and Worthington, S. (2012).*Gower & Davies: Principles of Modern Company Law,* 9th edition, Sweet and Maxwell, London, p. 509.
[21] Or insider trading, which is a situation whereby a company's insider, such as a director, having access to privileged information by virtue of his office, engages in profitable share transactions for his benefit.

insider dealing. Further, the power of directors to allot shares has now been greatly curtailed by statute, by requiring members to give periodic authorisation.[22]

Although directors do not owe duties to their company's employees, creditors and other such associates per se, they may still need to have regard to their interests under certain circumstances. This point is discussed further under **4.2.3**infra.

4.2.2 Duty to Act within Powers

The first of the duties recognised by the Act is that which requires the director to "act within powers".[23] This replaces the common law principle under which directors must act in accordance with the memorandum and articles and the proper purpose doctrine. To be more specific about the meaning of "powers" under the Act, it is stated that "a director of a company must (a) act in accordance with the company's constitution, and (b) only exercise powers for the purposes for which they are conferred".[24] Unlike the principle under common law, specific mention of the "memorandum" is omitted here because the Act has abolished the limitation on the powers of commercial companies. Thus, unless a company specifically elects to restrict its objects, it can generally decide to do any act which an individual can undertake.[25]

Further, "the company's constitution" has been defined under s.17 of the Act as including (a) the company's articles and (b) any resolutions or agreements specified in s.29.[26] These include special resolutions passed by the company and any resolutions and agreements that have been agreed to, or which otherwise bind classes of shareholders.

The reference to the company's constitution here as a document or act of the company that has the potential to restrict, or in some manner, define, the powers of the directors, has two important implications. Firstly, allowing this broad meaning for "the

[22] Refer to s. 551, generally.
[23] See s. 171
[24] Refer to s. 171.
[25] Refer to s. 31(1)
[26] See also s. 257.

constitution" is helpful in easing the decision-making process in companies. In order to check the directors, for instance, the shareholders need not always resort to the complicated process of altering the articles: they could simply take a decision in the general meeting giving the directors instructions to act in a certain way.[27]

Secondly, since the duty is captioned "to act within powers", the Act thereby implies that, in their responsibility of organising and administering the affairs of the company, it is essential for directors to familiarise themselves with the detailed contents of the company's "constitution" as defined under the Act, in order to know what their powers are and act within those limits. If the directors exercise a power so conferred for a purpose other than that for which, upon proper interpretation, it was conferred, this conduct could be open to challenge. They cannot claim to have acted with good intentions for the good of the company because prima facie, their powers must always be exercised within the limits specified for them.[28] Thus, the use of a power for a collateral purpose in the belief that it is in the best interest of the company, however well intentioned, is liable to be set aside, having been exercised for an improper purpose.[29]

The Act, rightly in this writer's view, does not attempt to set out what will qualify as proper purpose: this must be uniquely determined by every given set of circumstance. But clues can be found in previous case law. Generally, the courts refrain from substituting their own views for those of the boards as to the correctness of the

[27] This they can do even where the power in question was originally reserved exclusively for the directors by the articles. However, it cannot operate retroactively in order to invalidate a previously valid exercise of the directors' powers. The proposed model articles supported by the Companies Act (which are applicable to companies by default) make provision for this. See Article 4(1), Schedule 1 Regulation 2, Model Articles for Private Companies Limited by Shares and Article 4(1) Schedule 3 Regulation 4, Model Articles for Public Companies, effective from April 28, 2013.

[28] However, see s. 40 which is a presumption in favour of any person dealing with the company, that the directors' are not restricted in their powers.

[29] Refer to the statement of Parker J. in *RegentcrestPlc (In Liquidation) vs. Cohen* (2001) 2 BCLC 80, at 123.

boards' exercise of management powers. However, where on an objective review of the situation, the court finds that a requirement allegedly underlying the board's action was not urgent or critical, it may have reason to doubt or discount the assertions of the directors that they acted solely to deal with this requirement.[30]

Directors have variously been found to have wielded their powers *improperly* to cause the company to act ultra vires,[31] or pay dividends or directors remuneration contrary to the provisions of the company's articles.[32] However, one power of directors most often called to question in this regard is that for allotment of shares. Directors have more often wielded this in order to stave off a takeover[33] so as to perpetuate their posts, or favour one bidder over another for selfish interests.[34] Generally, the discussions earlier made under**3.5** in this work, apply here.

It is perhaps of particular importance to note that under the UK law as enacted, the courts would more probably need to consider not only an interpretation of a company's articles, but also any resolutions by members at the general meeting, in order to determine at any particular point, whether any act of the directors was in fact ultra vires their powers. This is because it is actually possible for the members in a resolution, to authorise the directors to carry out an act which would otherwise be considered an improper utilisation of the directors' powers. It is submitted that the Act, by allowing this possibility, has thereby augmented the powers of the members over the board.

[30]Birds, J., et al. (2011).*Boyle and Birds' Company Law.*8th edition, Jordan Publishing Limited, Bristol, pp. 631-632.
[31]*Re Lands Allotment Company* (1894) 1 Ch. 616 C.A.
[32]*Re Oxford Benefit Building and Investment Society* (1886) 35 Ch. D. 502.
[33]*Winthrop Investments Ltd. vs. Winns Ltd.* (1975) 2 N.S.W.L.R. 666, NSWCA.
[34]*Howard Smith Ltd. vs. Ampol Petroleum Ltd.* (1974) A.C. 821.

4.2.3 Duty to Promote the Success of the Company

This duty is considered the foremost fiduciary duty of directors.[35] It appears to be inextricably linked to the preceding two subheadings above. Thus, the directors must utilize their powers for the ultimate success of the company, which should result in benefit for its members. In other words, success of "the company" is the "proper purpose" for which directors must utilize their powers so that the company's members would benefit. As will be observed shortly, this duty to promote the company's success is related, though not entirely equivalent, to the common law duty to act bona fide in the best interests of the company.

In the last two decades, the West, particularly Britain and the United States, suffered a wave of major corporate failures[36] which many attributed to, among other causes, short-termism[37]—a corporate strategy that typically neglects the consideration of the long-term future of the company, in favour of satisfying the demand by investors for immediate returns in the present, such that stability and financial strength needed to endure economic cycles are sacrificed for immediate satisfaction.[38] Although the Companies Act was conceived a long time before this period, and so could not have set out to nip any such recurrence in the future[39]—the law came in force just in time to address the aftermath of the crisis. Thus, having considered that "the state of directors'

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[35]Birds, J. et al. op.cit.at p. 634; Davies, L.P. and Worthington, S. (2012).Op.cit. at p. 540.

[36]Such as the notorious Enron debacle.

[37] See Lipton, M., Mirvis, T. andLorsch, J. (2009) *The Proposed Shareholder Bill of Rights Act of 2009*, Harvard Law School Forum on Corporate Governance & Financial Regulation. Retrieved October 10, 2013 fromhttp://blogs.law.harvard.edu/corpgov/2009/05/12/the-proposed-%e2%80%9cshareholder-bill-of-rights-act-of-2009%e2%80%9d; Williams, C. (2006)A Tale of Two Trajectories. *FordhamLaw Review,*75: 1629 at 1654-1655; Sharpe, N. (2010) Rethinking the Board Function in the Wake of the 2008 Financial Crisis*. Journal of Business and Technology Law 5:* 99 at 110-111; Grinyer, J. et al, (1998)Evidence of Managerial Short-termism in the UK. *British Journal ofManagement* 9*:* 13 at 14-15.

[38] It has been said that to apply a short-term approach strictly would mean that directors would be paying out to shareholders every amount earned as profit and with no consideration of investing funds and expansion of the company's market. See Heydon, J. *Directors' Duties and the Company's Interests*. In Finn, P. (ed), Equity and Commercial Relationships, Law Book Co., Sydney (1987) at 135.

[39]Keay, A. (2010)*The Duty to Promote the Success of the Company: Is it Fit for Purpose?* Working Paper, Centre for Business Law and Practice, School of Law, University of Leeds, England, p. 5.Retrieved October 21, 2013 fromhttp://papers.ssrn.com/sol3/papers.cfm?abstract_id=1662411.

duties at common law are often regarded as leading to directors having an undue focus on the short term and the narrow interests of members at the expense of what is in a broader and a longer term sense the best interests of the enterprise,"[40] the Company Law Review Steering Group (CLRSG)—created by the then Department of Trade and Industry(DTI), now Department of Business, Enterprise and Regulatory Reform (DBERR)—saddled with the responsibility of proposing reforms for adoption by Parliament, proposed a solution. S. 172 was suggested as having the potential to prevent such corporate failures as well as the attendant devastating consequences. Therein is stated the modern objective of the corporation vis a vis its relationship with members on the one hand and subjects other than members, on the other. Prior to the Companies Act 2006, there had been no definitive legislative statement establishing the core objective of the UK 'corporation'. A determination of the scope of company law and governance—i.e. in whose interests companies should be run—was, therefore, a critical aspect of the reform agenda.[41]

During parliamentary debate leading up to the completion of the Companies Bill that culminated in the Act, therefore, the Berle-Dodd debate[42] was somewhat revived. Traditionally, directors had been required to exercise their powers simply in "the interests of the company." The latter was believed to be akin to the interests of both present and future members,[43] since it was understood as technically impossible to assign any interests to the artificial entity called "the company" by itself, without relating it to the interests of human persons. The contention had been whether to simply

[40] Company Law Review *Modern Company Law for a Competitive Economy*: The Strategic Framework (1999) Department of Trade and Industry (DTI) London, at para 5.1.17.
[41] Tate, C.R. (2011).*S.172 CA 2006: The Ticket to Stakeholder Value or Simply Tokenism?* Being term paper submitted to the Graduate School of Law, University of Aberdeen p. 1, citing Modern Company Law for a Competitive Economy: The Strategic Framework, CLRSG (February, 1999), para 5.1.4-5.1.33.
[42] Refer extensively to **3.4.2** in the previous chapter of this work on "In whose Interests and for whose Benefit should Directors Manage the Company?" for a fuller discussion.
[43]*Brady vs. Brady* (1987) 3 BCC, 535 at 552 (CA); *Gaiman vs. National Association for Mental Health* (1971) Ch. at 330.

codify this traditional notion, thereby adopting a *shareholder primacy* attitude or whether to give equal status to all the company's numerous stakeholders and thereby accept the *pluralist* corporate ideology increasingly popularised by business schools.

In rejecting the latter two and finally settling for the contents of s. 172, Parliament thereby introduced what the CLRSG dubbed *enlightened shareholder value* (ESV) approach. The section in part provides that

> *(1)A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—*
> *(a) the likely consequences of any decision in the long term,*
> *(b) the interests of the company's employees,*
> *(c) the need to foster the company's business relationships with suppliers, customers and others,*
> *(d) the impact of the company's operations on the community and the environment,*
> *(e)the desirability of the company maintaining a reputation for high standards of business conduct, and*
> (f) *the need to act fairly as between members of the company.*

By this provision, the law makers attempted to avoid taking sides in the Berle-Dodd debate earlier discussed by seeking a middle course, although undoubtedly one closer to Berle's view, considered the traditional shareholder primacy model.[44] This is evident in the statement "for the benefit of its members as a whole," which comes first before *having regard* to the items mentioned in subsection 1 (a) to (e) above. However, the pluralist approach, which might have given all stakeholders equivalent status by allowing all to enforce directors' duties, was rejected. But the drafters still lent credence, albeit a modest one, to Dodd's side of the argument by recognising other

[44]Davies, L.P. and Worthington, S. (2012).Op.cit. at p. 541.

interests apart from a company's members. This adoption of aspects of both views in a holistic manner is what Parliament intended as the principle of ESV.

Policy makers consisting of the members of the committee of the CLRSG of England, in making their recommendations for the companies bill, saw the overall objective of codifying the directors duties as one of achieving a "shareholder oriented, but inclusively framed, duty of loyalty", which involved the recognition that, whilst the objective of directors was to act in the collective best interest of shareholders, this could only be achieved by taking due account of wider interests.[45] This policy essentially combines aspects of the traditional shareholder primacy with those of the pluralist, stakeholder management model. In the words of the CLRSG, the ESV is "a hybrid of the two approaches which maintains the primacy of shareholders but requires long term approach and permits directors to consider other interests as the best way of securing prosperity and welfare overall."[46]

The committee was of the view that this approach would better achieve wealth generation and competitiveness by discouraging the exclusive focus on the short-term financial bottom line widely believed to have caused corporate failures and instead, advocating a more inclusive approach that values the building of long-term relationships,[47] so that a balance is struck between the competing interests of different stakeholders, in order to benefit the company's shareholders in the long run.[48] It is

[45]*Developing the Framework,* (March, 2000).A report of the Company Law Review Steering Group (CLRSG), published by the Department of Trade and Industry, paragraph 2.22.Retrieved October 10, 2013 fromhttp://www.berr.gov.uk/bbf/co-act-2006/clr-review/page25086.html.

[46] Modern Company Law for a Competitive Economy: The Strategic Framework, a report of the Company Law Review Steering Group (CLRSG) (1999), para 5.1.12. It can be accessed at http://www.berr.gov.uk/files/file23279.pdf.

[47]*Developing the Framework,* a report of the Company Law Review Steering Group (CLRSG), published March, 2000, paragraph 2.22. It can be accessed at http://www.berr.gov.uk/bbf/co-act-2006/clr-review/page25086.html.

[48]Armour, J. et al. (2003) Shareholder Primacy and the Trajectory of UK Corporate Governance.*British Journal of Industrial Relations*, 41: 531 at p. 537; cited in: Keay, A. (2007). Tackling the Issue of the

hoped that this would make the process of management more enlightened and encourage more responsible decision-making that would avert corporate failure. Hodge MP,[49]remarked regarding s. 172, that the provision therein "marks a radical departure in articulating the connection between what is good for a company and what is good for society at large.[50]

The otherwise ineffectual provision for non-shareholder stakeholders in s. 172 is fortified by a further requirement under s. 417 for a business review[51] by directors of large or quoted companies. This must state how, if at all, they have performed their duty under s.172, to be presented before the general meeting as part of the (annual) directors' report. By this, Parliament intends that directors should consciously advert their minds to the requirements under the section and justify their decisions, presumably, by presenting "evidence" of their thought process, to show that they have in fact done so. However, the members are the likely recipients of the information contained in the directors' report: the stakeholders listed have therefore, no means of coming to the information contained therein.

There has been much speculation concerning the proper interpretation and effectiveness of s.172 due to its novelty and partly because it is not so closely aligned with a previous duty as are other duties provided in the Act.[52]The fact that very few courts have so far had the chance to interpret the duty in their deliberations, has not been helpful.However, commentators have since been advancing their views. Many[53]are

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Corporate Objective: An Analysis of the United Kingdom's Enlightened Shareholder Value Approach.*Sydney Law Review.* 29: 577-612, at 590.

[49] Also the Minister of State for Industry at the time of enacting the new companies law.

[50]*Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007), p. 3, accessible at http://www.berr.gov.uk/files/file40139.pdf.

[51]So-called non-financial disclosure.

[52]Keay, A. (2010)op.cit.atp. 5.

[53] Including Lord Glennie in *Re West Coast Capital (LIOS) Ltd*. (2008) CSOH, 72; 2008 Scot (D) 16/5 (Outer House, Court of Sessions, Lord Glennie at 21; Warren J. in *Cobden Investments Ltd. vs. RWM Rangport Ltd*. (2008) EWHC 2810, (Ch); Birds, J. et al. op.cit. at pp. 637-638; Davies, L.P. and Worthington, S.

of the opinion that not much has been changed from the closest common law antecedent of the duty and that whatever development made thereto is, at best, modest.

As famously demonstrated by the decision in **Re Smith & Fawcett**[54] directors were formerly required to act "bona fide in what they consider—not what the court may consider—is in the interests of the company",[55] so that the issue of reasonableness would never arise.[56] Provided directors believed in good faith to be doing what they thought to be best for the company, their actions were safe from court scrutiny. In fact, the courts took the subjectivity yardstick to such levels that not only did they decline to impose their own views as to whether the decisions made by the director were in the best interests of the company,[57] but also refused to hold a director liable simply based on the fact that a particular decision he took happened to result in injury to the company.[58] However, in all instances, the proper purpose doctrine took precedence over the bona fide rule. Thus, directors would only be exonerated where they had exercised their powers for the proper purpose, in the first place. Here, the dictum of Parker J. is particularly apposite:

> *The duty imposed on directors to act bona fide in the interests of the company is a subjective one… The question is not whether viewed objectively by the court, the particular act or omission which is challenged was in fact in the interests of the company; still less is the question whether the court, had it been in the position of the director at the*

(2012).Op.cit. at p. 543; Tate, C.R. *op.cit.*at pp. 2, 3 and 8; Keay, A. (2007). Op.cit. at pp. 604, 610 and 611.

[54]Supra.

[55]Per Lord Greene M.R. in *Re Smith & Fawcett Ltd.* (1942) Ch. 304 at 306. See also the relatively more recent cases of *Clemens vs. Clemens Bros Ltd.* (1976) 2 All ER 268, at 268-280; *RegentcrestPlc (in liquidation) vs. Cohen* (2001) 2 BCLC 80 and *Extrasure Travel Insurances Ltd. vs. Scattergood* (2003) 1 BCLC 598, at 90.

[56] However, cf. the decision of Arden, L.J. in *Item Software (UK) Ltd. vs. Fassihi* (2005) 2 B.C.L.C. 91, that if a director embarks on a course of action without considering the interests of the company and there is no basis on which he or she could *reasonably* have come to the conclusion that it was in the interests of the company, the director will be in breach.

[57]*Re Smith & Fawcett Ltd.* (1942) Ch. 304 at 306; *RegentcrestPlc (in liquidation) vs. Cohen* (2001) 2 BCLC 80 and *Extrasure Travel Insurances Ltd. vs. Scattergood* (2003) 1 BCLC 598, at 90.

[58]*Extrasure Travel Insurances Ltd. vs. Scattergood* (2003) 1 BCLC 598, at 90.

> *relevant time, might have acted differently. Rather, the question is whether the director honestly believed that his act or omission was in the interests of the company. The issue is as to the director's state of mind. No doubt where it is clear that the act or omission under challenge resulted in substantial detriment to the company, the director will have a harder task persuading the court that he honestly believed it to be in the company's interests; but that does not detract from the subjective nature of the test…*
> *The position is different where a power conferred on a director is used for a collateral purpose. In such circumstances it matters not whether the director honestly believed that in exercising the power as he did he was acting in the interests of the company; the power having been exercised for an improper purpose, its exercise will be liable to be set aside…"*[59]

There is some evidence that the duty as provided under s.172 would be interpreted in much the same way as under common law, at least, when it comes to the standard required in decision-making. Apart from the fact that s.170(4) already endorses common law interpretation, familiar wordings used in s. 172, such as "in the way he considers," "in good faith" and "promote...the company" prompt such a conclusion. In fact, Hodge MP believed it "...essential for the weight given to any factor to be a matter for the director's good faith judgement. Importantly, the decision is not subject to the reasonableness test..."[60]

Certainly, the courts have taken the hint that the director is still allowed this discretion to decide how best to achieve the objective in s.172; he still has a right to his business judgment. The English High Court ruled the duty therein to be subjective, just like its precursor.[61] This position has so far consistently been maintained by the same

[59] *RegentcrestPlc (in liquidation) vs. Cohen* (2001) 2 BCLC 80 at 120 and 123.
[60] House of Commons (HC) Standing Committee D, 5th Sitting, July 11, 2006, Cols 591-593.
[61] *Cobden Investments Ltd. vs. RWM Rangport Ltd*. (2008) EWHC 2810 (Ch.) at 53.

court,[62] so that the court would still not interfere with the director's good faith judgment in the best interests of the company, as under common law, if there was, prima facie, no reason to believe that he had acted mala fide, even where this results in consequences which are not in the company's favour, which was the case in **Shepherd vs. Williamson**.[63] There, the plaintiff was one of two directors as well as shareholders in a construction company. The company had been a bidder regarding a construction contract for a hotel chain. The Office of Fair Trading (OFT) had earlier launched an investigation into collusive practices in the construction industry. One of those practices was the giving and taking of "covers," that is to say, deliberately submitting a bid higher than other competing bids for a contract in the knowledge that it would not succeed, with the object of favouring a chosen tenderer amongst those colluding. Aware that the company was a subject of the ongoing OFT investigation, when the plaintiff discovered that the company was involved in a cover regarding the hotel contract bid, he blew the whistle through an anonymous phone call placed to the senior project manager of the hotel.Angered by this, the defendant, the only other director and shareholder of the company, proceeded to exclude the plaintiff from the affairs of the company, alleging that the plaintiff had all the while acted in bad faith by attempting to jeopardize its business interests.

In a petition brought by the plaintiff against the defendant for his shares to be compulsorily bought at a fair price, citing unfair prejudice, the court made its findings as to his motives and concluded that he had acted in good faith and in the interest of the company in exposing the unfair practice. Mrs Justice Proudman ruled that

[62] *Shepherd vs. Williamson* (2010) EWHC 2375, Ch. An electronic copy of the judgment can be accessed at http://www.bailii.org/ew/cases/EWHC/Ch/2010/2375.html, last visited October 23, 2013. The court cited the cases of *Re Smith and Fawcett Ltd.* (1942) Ch. 304; *Re Regentcrest Plc. vs. Cohen* (2001) 2 BCLC 80; and *Extrasure Travel Insurance Ltd. vs. Scattergood* (2003) 1 BCLC 598, Ch.D., with approval.

[63] (2010) EWHC 2375, Ch.

> *Applying the criteria laid down in s. 172, Mr Shepherd was balancing the deleterious consequences of his conduct as far as its relations with its major customer was concerned, and the potential for damage to the Company's employees if the contract was not gained, (s. 172 (1) (a) (b) and (c)), against the Company's reputation as a whole (s. 172(1)(d) and (e)) in the light of the OFT investigation. The decision as to what promotes the success of the Company within s. 172(1) is one for a director's subjective judgment, exercised in good faith...In my judgment Mr Shepherd cannot be criticised for wanting to ensure that the contract was not obtained by the use of collusive activities, irrespective of whether it meant that the Company might lose the contract altogether.*[64]

Conclusively, if a director can justify his actions under s.172, he cannot be found to be in breach of his duty to act in the best interests of the company. A fortiori, securing a contract or improving profit cannot be a defence to contravening any law or public policy. The fact that they benefit from the success of the company should not encourage a director to jettison the items in s.172 in order to please shareholders. The idea, as earlier stated, is to always consider the long-term consequences. Yet, it has been suggested that the reference by the section to "the long-term" does not mean that the directors cannot focus on the short term if they believe bona fide that it will promote the success of the company for the benefit of its members.[65]

But what does Parliament mean by "success" in relation to the company and how is it to be determined? Can it be rated purely on financial terms? In answer to the question posed, Lord Goldsmith of the Lords Grand Committee of Parliament suggested that

> *The starting point is that it is essentially for the members of the company to define the objective they wish to achieve. Success means what the members collectively want the company to achieve. For a*

[64]Ibid., at paragraphs 103-104.
[65]Keay, A. (2010) op.cit.atp. 25.

> *commercial company, success will usually mean long-term increase in value. but the company's constitution and decisions made under it may also lay down the appropriate success model for the company...For certain companies, such as charities and community interest companies, it will mean the attainment of the objectives for which the company has been established.*[66]

Although most companies are usually set up for the benefit of members, s. 172(2) recognises the peculiarity of charitable or other altruistic companies in having objectives other than benefiting members. Apart from such designated companies, however, the vast majority which are commercially inclined can venture into anything. Indeed, the Act abolishes the need for companies to state their objective in the memorandum: unless a company's articles specifically restrict the objects of the company, its objects are unrestricted.[67] Thus members can, through resolutions, decide at every turn, what the company should aim to achieve.

Lord Goldsmith's suggestion that *success for a commercial company will usually mean long-term increase in value*, is an attempt to draw attention to the ESV principle promoted by the section, so that shareholders would not always be looking to lay their hands on profit at the slightest opportunity but instead, consider the long-term implications of their demands on the company. Accordingly, the legitimate aim of maximising shareholder wealth should be tempered with an express acknowledgement that any company's prospects of success are dependent on its effective management of the various risks that confront it along the way.[68] It is intended that this *decision* as to what will promote the success of the company, and *what constitutes such success* on

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[66] *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 9, quoting the Hansard of February 6, 2006, column 255, accessible at http://www.berr.gov.uk/files/file40139.pdf.

[67] Refer to s. 31.

[68] Davies, J. *A Guide to Directors' Responsibilities Under the Companies Act 2006,* Certified Accountants Educational Trust, (2007), p. 29. Retrieved from http://www.accaglobal.com/content/dam/acca/global/PDF-technical/business-law/tech-tp-cdd.pdf, accessed March 27, 2013.

these terms, is one for the *directors' good faith judgement*,[69] after having regard to the company's constitution, shareholder decisions and anything else they consider relevant in helping them to reach that judgment.[70] The directors' interpretation of any business objectives could be important. It might be argued that what is done to fulfil that interpretation cannot be impugned provided that it cannot be established that the directors did not in fact have a good faith belief in the strategy they had adopted for promoting the company's success.[71]

Previously, the director was required to consider the "best interests" of the company and, as earlier stated, this was usually equated with the interests of both present and future members. Thus, transforming this to "benefit of members as a whole" would tend to be logical and judicially proper. The statement also appears to embrace future shareholders as well, just as it did under common law.[72] A fortiori, the CLRSG cautioned that directors should not, in the course of their duties, ignore events that may occur after the present members have ceased being members.[73]

As for the factors listed in s. 172 (1)(a)-(f), particularly factors (b), (c) and (d), common law decisions suggest that nothing previously prevented directors from considering them or any others, provided they could justify their decisions as being in

[69] *Shepherd vs. Williamsonsupra.* See also explanatory notes to the Companies Act 2006 at para 327.
[70] Per Lord Goldsmith of the Lords Grand Committee. See *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 10, quoting the Hansard of February 6, 2006, column 256, accessible at http://www.berr.gov.uk/files/file40139.pdf.
[71] Keay, A. (2010) op.cit.atp. 15.
[72] Again, Lord Goldsmith clarified here that Parliament intends the duty to be in the interest of "members as a collective body," not only to benefit the majority shareholders or any particular shareholder or section of shareholders, nor less still the interests of directors who happen to be shareholders.See *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 10, quoting the Hansard of February 6, 2006, column 256, accessible at http://www.berr.gov.uk/files/file40139.pdf.
[73] *Modern Company Law for a Competitive Economy: Developing the Framework*, a publication of the DTI, London (2000), para 3.54, accessible at http://www.berr.gov.uk/files/file23279.pdf.

the best interests of the company.[74] This is summed up in the famous dictum of Bowen L.J. that"the law does not say that there are to be no cakes and ale, but there are to be no cakes and ale except such as are required for the benefit of the company."[75] The same idea informs the decision in **Re W & M Roith Ltd.**,[76]where the court refused to allow an agreement between the company and its director—in which the company agreed to provide his widow with a pension for life—since there was nothing to be gained by the company in return. In these decisions and many others,[77] the court implied that, were the directors to have shown the real corporate benefits to be gained from their decisions, they could have succeeded.

S.172(1) went extra, not only in listing a number of items considered particularly important to any company, but also in making it an obligation upon the directors to "have regard" to them.[78] This is the novelty behind the section; what differentiates it from the common law rule or even any similar rule in any Commonwealth jurisdiction. Thus, previously, directors could consider *any* factor but now, they *must* consider at least the listed factors, along with any others they might wish to. This is because Parliament is of the view that business judgment is *enlightened* when it proceeds on the basis that a company's potential for success can best be realised through maximising the relationships which the company enjoys with stakeholder groups.[79] Those listed under the section are not exhaustive, but merely to be considered "among other matters" that may be relevant to any particular company.

[74]Birds, J. et al. op.cit.at 637. It has also been argued that the listing of these factors is merely an attempt to "introduce a stakeholder theory by the backdoor". See Woodley, J. op.cit. p. 62.
[75]*Hutton vs. West Cork Railway* (1883) 23 Ch. D. 654 at 673.
[76] (1967) 1 W.L.R. 432
[77]Such as *Parke vs. Daily News* (1962) Ch. 927 and *Dodge vs. Ford Motor Co*. (1919) 170 N.W. 668.
[78]Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 545.
[79]Arden, D.B.E. (2007). Companies' Act 2006 (UK): A New Approach to Directors' Duties. *Australia Law Journal,*81: 162-179, at 165.

An interesting question is, what does Parliament really intend by "have regard to" with respect to all the items it took pains to mention? Hodge MP had occasion to clarify that

> *The words "have regard to" mean "think about"; they are absolutely not about just ticking boxes. If "thinking about" leads to the conclusion, as we believe it will in many cases, that the proper course is to act positively to achieve the objectives in the clause, that will be what the director's duty is. In other words "have regard to" means "give proper consideration to…"*[80]

Essentially, therefore, the law relies on the director's good faith to discharge his obligations here.

Creditors do not specifically make the list in s. 172(1), although they may well be accommodated under "others" in item (c). It has been suggested that this omission should not be alarming considering the fact that, so long as a company's business is flourishing, its creditors position is not thereby compromised and besides, their contractual rights against the company plus the company's desire to preserve its reputation and access to future credit, will all act to protect the creditors.[81] However, s. 172(3) qualifies the duty to promote the success of the company for its members, by preserving any rule of law or statute that requires directors to consider the interest of creditors "in certain circumstances." This implies that a consideration of the interests of creditors may not be necessary under *all* circumstances. Situations likely to warrant such consideration would undoubtedly include instances where the company is facing financial difficulties, or 'doubtfully solvent,'[82] at which time the creditors' interests

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[80] *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 11, quoting Hodge MP in the Commons Report of October 17 2006, Column 789 of the Hansard, accessible at http://www.berr.gov.uk/files/file40139.pdf.

[81] Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 553.

[82] *Brady vs. Brady* (1988) BCLC 20.

become paramount.[83] Wrongful trading is thus, prohibited. Directors are guilty of "wrongful trading" if they allow the company to continue to conduct business and incur debts when there is no reasonable prospect of the company repaying the debt. There is no need for proof of intent for wrongful trading: the test is whether the director knew or ought to have known that there was no reasonable prospect of the company getting out of its financial difficulties.S. 214 of the Insolvency Act 1986 reinforces the rule that once it is clear that a company is no longer a going concern, a duty to creditors replaces any duty to shareholders.[84] It is pertinent to also note that creditors have power, through insolvency procedures, to control the company's assets which are, after all, theirs and not the shareholders'.[85]

Most of the factors listed in s. 172(1) are alien to UK company law, except (b), which mentions the interests of employees. Hitherto, s.309 of the Companies Act of 1985 had provided that the matters to which directors were to have regard in the performance of their functions included the "interests of the company's employees in general, as well as the interests of its members." Although this statement seemed to have created a parallel duty to consider interests of members and employees, still it has been argued that the provision had no significant impact on the decisions of directors because the interests of employees were still subordinate to those of members.[86] It was also regarded as simply creating a defence for directors who might have allowed employees' interests to override those of members.[87] Hoffmann J did hold some directors not liable for favouring the sale of their company's business to a party

[83] See *Lonrho Ltd. vs. Shell Petroleum Ltd.* (1980) 1 WLR 627, at 634 (HL), per Lord Diplock; *West Mercia Safetyware Ltd. vs. Dodd* (1988) BCLC 250, at 252-253 (CA), per Dillon LJ; *Brady vs. Brady* (1989) AC 755 (HL); *Singla vs. Hedman* (2010) 2 BCLC 61 at para 33 and *Roberts vs. Frohlich* (2011) EWHC 257 (Ch).

[84]Alcock, A. (2009)An Accidental Change to Directors' Duties?*Company Lawyer*, 362, p. 7. RetrievedNovember 11, 2013 from http://usir.salford.ac.uk/3112/1/CA_2006.pdf.

[85]Wild, C. and Weinstein, S. (2009).*Smith & Keenan's Company Law.*14th edition, Pearson Education Limited, England, p.345.

[86] See Birds, J. et al. op.cit. atp.637.

[87]Alcock, A. *op.cit.*p. 6.

prepared to take on the employees rather than to a party prepared to offer a higher price but without the employees.[88] Therefore, the provision indeed worked to exonerate the directors.

A similar provision is conspicuously absent in the present Act. It has been argued that the position of employees, rather than being improved upon, has in fact been weakened further by simply merging them with the other factors in s.172,[89] so that employee interests are now to be considered only to the extent that they promote company success for members benefit.[90] Still, a company which desires to, may provide for employees upon cessation or transfer of business[91] and even arrange employee share schemes.[92]

In spite of the numerous stakeholders listed in the section, however, the duty is still one owed the company[93] and none other, just as under common law. Hodge MP has clarified the intention of Parliament that, "while a director must have regard to the various factors stated, that requirement is subordinate to the overriding duty to promote the success of the company."[94] Thus, stakeholder interests have no independent value in the consideration of a particular course of action.[95] Consequently, only the company, or its members acting in its name, can enforce the duty. The stakeholders therein cannot do so beyond any independent contract they may have with the company.[96] This fact supports the argument that s. 172 merely reiterates, rather than changes, the prevailing

[88] *Re Welfab Engineers Ltd*. (1990) BCLC 833.
[89] Chohan, A.*Is S.172 of the Companies Act 2006 Capable of Delivering for All Stakeholders?*(2012) p.3 Retrieved July 3, 2013 from http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2139528.
[90] Davies, L.P. and Worthington, S. (2012).op.cit. at p.552; Worthington, S. (2001). *Reforming Directors' Duties*, London School of Economics (LSE) Research Online p. 8, accessed October 25, 2013 at http://eprints.lse.ac.uk/200/1/FinalMLRDDuties.pdf.
[91] Refer to s. 247.
[92] Refer generally to ss. 549(2)(a) and 1166.
[93] See s.170(1).
[94] Statement made by the Minister for Industry and the Regions in the course of Parliamentary debates.
[95] Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 542; Davies,P. and Rickford, J. (2008).An Introduction to the New UK Companies Act.*European Company and Financial Law Review*,5: 48 at 66.
[96] Unless they also happen to be members or directors in the company. See Keay, A. (2010) op.cit. atpp. 27-28.

shareholder-oriented approach to company law and governance.[97] This is more so when the important question is considered: can the court entertain the question whether or not directors have indeed taken account of the factors listed in s. 172 in order to decide if they have been in breach? The answer to this must take into consideration two facts already noted: a) the director is still entitled to his subjective business judgment and b) the duty is owed to none other than the company.

Under common law, cases regarding the proper purpose doctrine show that a director may breach the duty of acting in the interest of the company if it appears to the court that he failed to direct his mind *at all* to the question whether a transaction was in fact in the interests of the company, even though a board which had considered the question might have acted in the same way. This would especially be the case where there is no apparent corporate benefit to be realised from the director's actions.[98] Thus, it can safely be assumed—in the absence of judicial authority so far on the issue—that directors would not be found to be in breach of the duty simply because they did not give explicit thought to the factors listed under the section, unless it can be shown that some corporate loss had also been recorded due to such *disregard*.[99] Quite possibly, therefore, directors' decisions are likely to be open to some form of challenge under s. 172 only if and when the company goes into liquidation.[100]

The Act is not explicit about how boards of directors should reflect their compliance (or otherwise) with s.172, apart from the business review in the directors' report required of certain categories of companies under s.417.[101] However, it has been

[97]Tate, R. op.cit.at p.3.
[98] See for instance the cases of *Re W & M Roith Ltd*. (1967) 1 W.L.R. 432; *Parke vs. Daily News* (1962) Ch. 927; *Dodge vs. Ford Motor Co*. (1919) 170 N.W. 668.
[99]Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 547.
[100]Birds, J. et al. op.cit.at p. 638.
[101] This review is only required of large or quoted companies. Being part of the directors' report, it is mostly for the consumption of shareholders and debenture holders. Thus, other stakeholders mentioned in s. 172 have no access to it as of right, especially in large companies that are not quoted.

suggested that it may be in the interest of directors to make certain that the minutes of board meetings record the fact that the listed factors were indeed deliberated upon before any decisions were taken,[102] as directors would find it far easier to defend themselves against allegations of breach if they can present some evidence that they were all the while striving to comply with the statutory procedure.[103] Where matters arise that call on directors to make a conscious decision as to which of a number of competing and apparently mutually-exclusive factors to favour – for example the interests of the company's employees against the impact of the company's operations on the environment – directors may also find it useful to record the reasons why any particular option was considered to be the more likely to promote the success of the company.[104]

Yet, others argue that only a minority of directors' decisions are made at board meetings any way[105] and board minutes usually only record decisions and are not so detailed as to how such decisions were arrived at.[106] A fortiori, s. 309 of the Companies Act 1985 had for many years required directors to consider the interests of employees while discharging their duties to the company, yet this requirement has not led company boards to feel obliged to expressly cross-refer to this provision in board minutes,[107] nor have the courts found them in breach simply for that reason.

In any case, Hodge MP has also clarified even before the present law came in force that "the clause does not impose a requirement on directors to keep records, as

[102]Arden, D.B.E. op.cit.at 168;Keay, A. (2010) op.cit., p. 31; Davies, J. op.cit. p. 37
[103]Davies, J. op.cit.at 37.
[104] Ibid.
[105]Finch, V. (1992).Company Directors: Who Cares About Skill and Care?*Modern Law Review*55(2): 179 at 197. It was observed that most decisions taken in effecting company business are made by the Managing Directors or individual directors and it is usual for the articles to sanction this. See alsoLumb, L. Blankfield, A. (2010)*Directors' Duties, Companies Act 2006: Restatement or Substantive Change?* Field Fisher Waterhouse LLP, England, p. 7. Retrieved March 26, 2013from http://www.ffw.com/pdf/Directors-duties.pdf.
[106]Davies, J. op.cit. at p. 37
[107]Ibid.Also,Lumb, L. and Blankfield, A. *op.cit.*at p. 7.

some people have suggested, in any circumstances in which they would not have to do so now."[108] Responding to fears that the section may cause increase in litigation, Parliament allayed fears by also stating that it didn't think that would be the case, considering the fact that having to consider the interests of employees had been in the law for a long time yet, has hardly ever led to litigation.[109] In essence, Parliament was conceding that the section would be difficult to litigate!

In spite of the attempt by Parliament to tread a middle path, proponents of both shareholder and stakeholder business theories have criticised the general tenor of the section. Shareholder primacy advocates on their part point to the fact that the law thereby proposes to teach businessmen how they should make business decisions[110]by venturing to state what they must think,[111] when this should have been the proper purview of business schools and voluntary corporate codes of ethics.[112] Besides, critics doubt that the section would in any way improve quality of decision making or cause directors to change the way they manage enterprises.[113] Further, there is the question of the mode of deciding between two or more conflicting stakeholder interests.[114] Most of all, some argue that the section as drafted would only serve as escape route for directors

[108]*Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 10, quoting the Hansard of the Commons Committee of July 11 2006, column 292, accessible at http://www.berr.gov.uk/files/file40139.pdf.

[109]*Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 10, quoting Lord Goldsmith MP of the Lords Grand Committee, from the Hansard of February 6 2006, column 243, accessible at http://www.berr.gov.uk/files/file40139.pdf.

[110]Hollington R. (2008).*Directors' Duties under the Companies Act 2006: Have the Lunatics Taken Over the Asylum?* A lecture delivered at Ian Fairbairn Lecture Theatre, University of Buckingham, (April 22, 2008), pp. 4 and 7.Retrieved March 23 2013 from http://www.newsquarechambers.co.uk/files/Publications/Directors%20duties%20under%20the%20Companies%20Act%202006%20(Robin%20Hollington%20QC).pdf.

[111] Ibid. at p. 1

[112] Ibid. at p. 7

[113]*The Social Responsibility of Corporations 2006*, a report of the Australian Corporations and Markets Advisory Committee (CAMAC), at para 3.12. Cited in:Horrigan, B. (2012) Directors' Duties and Liabilities: Where Are We Now and Where Are We Going in the UK, Broader Commonwealth and Internationally? *International Journal of Business and Social Science,* 3(2): 21-45, at p.20

[114]Keay, A. (2010) op.cit atp. 18.

by allowing them defend a case of breach by asserting that their actions were guided by the need to consider the interests of non-shareholder stakeholders in order to promote the success of the company.[115]

Stakeholder theorists, on the other hand, lament the fact that stakeholders under the section are still relegated to second place relative to shareholders, and their interests are considered only to the extent that they serve the interests of shareholders.[116] In other words, the section still begins with a statement of shareholder primacy and so, given this strident affirmation of shareholder supremacy, as Alcocksuccinctly puts it, "what can the remainder of subsection (1) with its list of other interests really achieve?"[117]Besides, when the CLRSG was proposing the contents of s. 172 back in 1999, it did suggest that having regard to the listed interests is not based on fairness, but on efficiency and ensuring that shareholders get more, overall.[118]Further, some argue that the section as drafted would only encourage box-ticking and paying lip service to the items listed therein,[119] in spite of the fact that the government had clarified that the words "having regard to" mean "think about" and "are absolutely not about just ticking boxes."[120] Moreover, there is also the basic issue of enforcement: while shareholders can resort to the general meeting and derivative action, the other stakeholders have no

[115] Ibid. at35-36.

[116] In fact, it is believed that, in spite of the provision in s. 172, company directors still predominantly understand their fiduciary duties to be to the shareholders, with pressures from the capital markets and private equity shareholders underscoring that orientation. See Devinney, M.T.,Schwalbach, J. and Williams A.C. (eds.) (2013).Corporate Social Responsibility and Corporate Governance: Comparative Perspectives.*Editorial to Corporate Governance: An International Review*, 21(5): 413, at p. 414.

[117]Alcock, A.op.cit.at p. 12.

[118]The Company Law Review Steering Group, Department of Trade and Industry, *Modern Company Law for a Competitive Economy*: *The Strategic Framework* (1999) at 36-37, accessed November 17 at http://www.berr.gov.uk/files/file23279.pdf.

[119] Sykes (2010) p. 228

[120]*Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 11, Hodge MP in the Commons Report of October 17 2006, Column 789 of the Hansard, accessible at http://www.berr.gov.uk/files/file40139.pdf.

such means, leaving their fate simply in the hands of directors' good faith. Conclusively, therefore, the provision could end up pleasing no one.[121]

It has been argued that a broadly-formulated pluralist provision such as s. 172(1), cannot by itself operate to change the decision-making processes of a board unless this is coupled with further changes in company law, such as board-level representation for the relevant stakeholder groups.[122] Thus, the effect of the section is more likely to be educational, rather than in any sense restrictive and so business decisions taken in good faith will not be any more easily challengeable than they were before the provision existed.[123]It has therefore been suggested, and this writer tends to agree with the view, that the ESV principle introduced under s. 172(1) is at best a modest development of the common law,[124] highly unlikely to have any great impact on company boards and how they transact business.[125] Perhaps, this informs the reason why other jurisdictions, such as Australia, Singapore, Hong Kong, Malaysia, New Zealand, which usually follow the lead of UK legislations, hesitated when it came to s. 172 while reviewing their corporate legislations post 2006, even after due consideration.

4.2.4. Duty to Exercise Independent Judgment

Recently, owing in the most part to the spate of colossal corporate failures around the world, the phenomenon of having one or more independent non-executive directors on the boards of companies has gradually materialised in every standard code of corporate ethics. The UK Corporate Governance Code 2012 in particular requires at least half the board of listed companies to constitute independent non-executive directors. Part of the

[121]Keay, A. (2007).Op.cit. at p. 612. In fact, it is said that for directors, the effect is they may be doubly disadvantaged: if they pay too much attention to any one of the factors, they may be challenged for being in breach of the primary duty towards shareholders. On the other hand, if they ignore any of the factors and this proves disastrous for the company, they may be challenged for the breach of their duty to exercise reasonable care, skill and diligence. See Alcock, A. op.cit. at p. 15.
[122]Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 553.
[123]Birds, J. et al. op.cit.at p. 638.
[124]Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 543.
[125]Keay, A. (2010) op.cit.atp. 36.

aim is to ensure that, as much as possible, directors make business decisions with some detachment and for the sole purpose of the business only: they must not be encumbered by, or beholden to, anyone in any way. After all, "directors have but one master, the company."[126] This informs the duty imposed by s. 173 on all directors to exercise independence in judgement during the course of their duties.

At common law, a director is not allowed to "fetter" his discretion either to vote or to act in any manner. The principle obviously follows not only from the general duty to act in good faith but also the principles prohibiting conflicts of duty and interest, and requiring directors to exert reasonable care, skill and diligence. Consequently, a director cannot agree with any outsider to conduct himself in a manner favourable to the former in discharging his duties. As noted by Birds et al,[127] case law has established that it is not necessarily unlawful for a director to do this provided that he i) did not conceal his position ii); had the consent of the company;[128] iii) preserved a substantial degree of independent discretion as to how he would exercise his powers[129] and, iv) if a divergence occurred between the interests of the company and those of the 'outsider', did not subordinate the former to the latter as a means of resolving conflict.[130]

In an obvious attempt to clarify, modify and modernize this common law principle, s. 173 puts it better in positive terms[131] thus:

> *(1) A director of a company must exercise independent judgment.*
> *(2) This duty is not infringed by his acting—*
> *(a) in accordance with an agreement duly entered into by the companythat restricts the future exercise of discretion by its directors, or*
> *(b) in a way authorised by the company's constitution.*

[126]Per Lord Cullen in *Dawson International Plc. vs. Coats Patons Plc*. (1988) 4 B.C.C. 305 CS (OH).
[127]Birds, J. et al. op.cit.at p.639.
[128] See *Kregor vs. Hollins* (1913) 109 LT 225, at 231.
[129]*Boulting vs. ACTAT* (1963) 2 QB 606, at 626-627.
[130]*Scottish Co-operative Wholesale Society Ltd. vs. Meyer* (1959) AC 324.
[131]Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 536.

Noticeably, the law has spelt out the limit of independence required by stating instances where the duty would not be said to have been breached. This is considered necessary in the interest of business. During the passage of the Act through Parliament, the government clarified the ambit of the duty, stating that

> *...the clause does not mean that a director has to form his judgement totally independently from anyone or anything. It does not actually mean that the director has to be independent himself. He can have an interest in the matter…It is the exercise of the judgement of a director that must be independent in the sense of it being his own judgement…The duty does not prevent a director from relying on the advice or work of others, but the final judgement must be his responsibility. He clearly cannot be expected to do everything himself. Indeed, in certain circumstances directors may be in breach of duty if they fail to take appropriate advice – for example, legal advice. As with all advice, slavish reliance is not acceptable, and the obtaining of outside advice does not absolve directors from exercising their judgement on the basis of such advice.*[132]

Basically, the limits, both from case law and the Act, can be summarised thus:[133]

1. directors are not precluded from complying with contracts by which the company is bound;
2. exercise of independence can be jettisoned while acting in accordance with the company's constitution, orauthorisation thereunder;
3. delegating to appropriate individuals or committees is allowed where otherwise permitted;
4. relying upon advice in areas where this is required is permitted and even demanded, provided directors exercise their judgment in deciding whether to follow such advice.

It would be undesirable to prevent directors from undertaking to conduct themselves in the future in a way as to give effect to a contract they enter into on behalf of the company. A strict rule would have the potential of making companies unreliable contracting parties and even deprive them of the opportunity to enter into long-term

[132]Per Goldsmith MP of the Lords Grand Committee, recorded in the Hansard of February 6 2006, column 282.
[133]Lumb, L. Blankfield, A. *op.cit.*, p. 4.

contracts.[134] Besides, if the corporation is imbued with legal personality like natural persons, then it follows that corporations should likewise be able to contract as to their future behaviour. S.173(2)(a) codified the decision in **Cabra Estates Plc. vs. Fulham Football Club**,[135] wherein the directors of the respondent had entered into a contract for the development of a football ground with the appellant, undertaking that Fulham Football Club Ltd would not oppose the development contract at a later date or support a compulsory purchase order. It was held that the directors had not improperly restricted the future exercise of their discretion.

Once more, as is evident throughout the Act, the company's constitution is highly regarded. Recall that it is not restricted to the articles but includes any resolutions or agreements duly reached.[136] This essentially allows some measure of control over management and lends flexibility so that as the need arises, members can decide to allow directors act in an otherwise improper manner in order to achieve a certain goal or give effect to contractual obligations. This will be especially helpful in group situations. Where the constitution also permits delegation, the directors may resort to it, though even the decision to delegate, must be solely theirs.

Considering the fact that directors may need to constantly resort to the opinion or advice of experts, such as lawyers, valuers or auditors, the court would hardly find them in breach of the duty to exercise independent judgment because they do. In fact, it has been suggested[137] that directors may breach their duty to take reasonable care and act diligently if they fail to consult appropriate experts, although they must not treat any such opinion as an instruction, merely as advice they may or may not decide to adopt.

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[134]Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 538.

[135](1994) 1 BCLC 363, CA, following the Australian court's decision in *Thorby vs. Goldberg* (1964) 112 CLR, 597, Aust.HC.

[136] Refer to ss.17 and 29.

[137]Davies, L.P. and Worthington, S. (2012). Op.cit. p. 536.

The duty under consideration is of particular relevance in situations involving nominee directors who are often nominated by a shareholder, creditor or even an outsider to see to the latter's interests. Here, the director still cannot jettison the interests of the company in favour of those of his nominator[138] because, as Lord Cullen pointed out, he has only one master, the company,[139] which he must serve while employing only his own judgment. Besides, the nominator could be liable for the negligence of the director, if it can be shown that he/it had exploited this position and interfered with the affairs of the company.[140]

4.2.5. Duty to Exercise Reasonable Care, Skill and Diligence

Another area of considerable interest in the codification of directors' duties in the UK, is the standardization of the duty under this head. The director's duty of care and skill is simply a manifestation of the general duty of care imposed on all individuals in the conduct of activities, so that a person may be liable to pay compensation when found to have been negligent by causing harm to someone else.[141] It is this same principle that is extended to corporate law. Having a chequered history, the duty to exercise reasonable care, skill and diligence stems from the idea of company law having to balance the need for directorial accountability with the need to permit a certain amount of entrepreneurial risk taking.[142] On the one hand, the law ought to demand a certain amount of responsibility on the part of directors and on the other, creativity and initiative must not

[138] *Boulting vs. ACTT* (1963) 2 Q.B. 606 at 626, per Lord Denning M.R.; *Kuwait Asia Bank EC vs. National Mutual Life Nominees Ltd.* (1991) 1 A.C. 187, PC. But consider *Re Neath Rugby Ltd*. (2008) 1 BCLC 527, particularly at par. 26-27, where the court held that though the nominee's primary loyalty is to the company, he is entitled to have regard to the interests or requirements of his appointer to the extent that they are not incompatible with his primary duty to the company.

[139] *Dawson International Plc. vs. Coats Patons Plc*. (1988) 4 B.C.C. 305 CS (OH).

[140] *Kuwait Asia Bank EC vs. National Mutual Life Nominees Ltd.* (1991) 1 A.C. 187, PC.

[141] Worthington, S. op.cit., pp. 9-10.

[142] Roach, L. (1999).The Director's Duty of Skill and Care: Has the Law Commission Got it Right?*Business Law Review*, 20(51): p. 4. Retrieved December 11, 2013, from http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1754664. Indeed, some have gone as far as to say that "companies are in business to take risk." See Davies, L.P. and Worthington, S. (2012).Op.cit. at p. 522 and Worthington, S. op.cit., p. 10.

be stifled for they are the pillars of business ventures, which companies most often are. Still, risk taking by company management must be restricted to acceptable levels.

The duty applies to everything that directors do. The minimum degree of care, skill and diligence required, therefore, is what the law has been hard put to decide, over time. At first, the duty was judged by subjective standards and many court decisions in the late nineteenth and early twentieth century continuously endorsed this notion, some of the most notorious of which were**Re City Equitable Fire Insurance Co.**,[143]**Re Cardiff Savings Bank (Marquis of Bute's Case)**[144]and **Re Brazilian Rubber Plantation and Estates**.[145] The decision by Romer J.[146] neatly summed up what these cases proposed, namely that (i) the skill to be expected was merely what a person of the director's knowledge and experience could reasonably be expected to display; (ii) a director was not bound to give continuous attention to the affairs of the company; and (iii) a director could trust others entrusted with specific duties to perform them honestly in the absence of grounds for suspicion. The common law then seemed not to have distinguished between executive and non-executive directors when it came to the manner of discharging their duties. They were all judged by the same low, subjective standard. It is suggested that the courts may have been influenced by a model of corporate decision-making which gave the shareholders effective control over the choice of directors. Thus, if the shareholders chose incompetent directors, that was their fault. They must therefore bear the consequences.[147] Expectedly, the effect of such decisions was undesirable: directors were more or less immune from suit arising out of

[143](1925) Ch. 40.
[144](1892) Ch. 100.
[145](1911) 1 Ch. 425.
[146]Re City Equitable Fire Insurance Co. *supra*.
[147]*Turquand vs. Marshall* (1869) 4 Ch. App. 376.

their conduct of the entrepreneurial aspect of their functions.[148] It was thought that the common law gave directors a remarkable freedom to run companies incompetently.[149] For more discussions on these submissions and more, refer to **3.3** supra.

Criticism of the aforementioned decisions as well as a change in perception of company management[150] in time combined to force the hand of the courts to begin to take a harder look at, and demand a higher standard of, services rendered by directors. Beginning from the decision in**Dorchester Finance Co. Ltd vs. Stebbing,**[151]the common law standard for directors began to change. In that case, the plaintiff, which was a money lending company, had three directors, S, P and H. S was involved in the affairs of the company on a full-time basis, while P and H made only rare visits. S and P were qualified accountants and H, though in fact unqualified, also had considerable accountancy experience. At S' request, P and H signed blank cheques in the company's name which, unknown to them, enabled S to make unsecured loans to other persons and companies with whom he had some connection. Eventually, the loans could not be recovered by the company, which then brought an action against the three directors for alleged negligence and misappropriation of company's property.

Foster J. held all three liable, especially S who was said to have been grossly negligent. P and H were also held to have failed to exhibit the necessary skill and care in their duties even as non-executive directors. Apparently, it made no difference that the evidence showed that they had acted throughout in good faith. While their accountancy experience and qualification may have prompted the court to reach this

[148]Pettet, B. Common Law Duties of Care and Skill.Retrieved December 11, 2013, from http://law.oxy.co/common-law-duties-of-care-and-skill-93650/. This is coupled with the fact that shareholders are hampered by the rule in Foss vs. Harbottle in instituting actions against directors.
[149] Finch, V. Op.cit., at p. 179.
[150]Mainly arising from indications of a new statutory interest in responsible management and by developments at European Community level, in North America and in the Commonwealth.
[151] Decided in 1977, but reported much later: (1989) BCLC 498.

conclusion,[152] the judge stressed the fact that as far as directors duties were concerned, there was no distinction to be drawn between executive and non-executive directors. It can therefore not be said with certainty that the court would not have come to the same conclusion had the directors not been so qualified.

This was certainly a marked departure from the earlier cases of the late nineteenth century. Unlike the decision of Neville J.[153] that one could take up the directorship of a rubber company in complete ignorance of anything connected to rubber without accruing responsibility for any mistakes resulting from such ignorance, the English court in **Re Barings Plc. (No. 5)**,[154] ruled that "directors have, both collectively and individually, a continuing duty to acquire and maintain a sufficient knowledge and understanding of the company's business to enable them properly to discharge their duties as directors." Clearly, the courts were beginning to have a rethink of their past decisions.

Another case which at once showed a marked departure from the earlier common law position and set the format for the present standard under the Act, is **Norman vs. Theodore Goddard**[155] which was followed by **ReD'Jan of London Ltd.**,[156]all decided by the same judge, who held similarly in both cases that s. 214(4) of the Insolvency Act 1986 in relation to wrongful trading, properly expressed the standard to be expected of directors in the discharge of their duties. The said s. 214applies where a company has gone into insolvent liquidation and, at some time before the commencement of the winding up, a director knew or ought to have concluded that there was no reasonable prospect of avoiding insolvent liquidation. If the director does not convince the court that he took every step he ought to have taken to minimise the

[152]Wild, C. and Weinstein, S., op.cit.at p. 339; Finch V. Op.cit. at p. 201.
[153]*Re Brazilian Rubber Plantation and Estates* (1911) 1 Ch. 425.
[154](2000) 1 BCLC 523.
[155](1991) BCLC 1028.
[156](1993) BCC 646.

potential loss to creditors, personal contribution to the company's assets may be ordered.S.214(4)judges the steps to be taken or conclusions to be reached by both objective and subjective criteria. The director's actions or conclusions are judged by those of a reasonably diligent person who has both the general knowledge, skill and experience reasonably expected of a person carrying out the same functions as that director *and*the general knowledge, skill and experience that that director actually has. Thus, it has been suggested[157] that the honest incompetent and the unjustified optimist may now have something to fear.

Thus, the court resorted to the Insolvency Act in order to define the standards in evaluating the conduct of the directors. Apparently, the English Law Commission and the CLRSG considered the court's decision to have been properly reached, so that "it is now accepted that the duty of care…is accurately stated in s.214(4) of the Insolvency Act 1986,"[158] and confirmed in s. 174 thus:

> *(1) A director of a company must exercise reasonable care, skill and diligence.*
> *(2) This means the care, skill and diligence that would be exercised by a reasonably diligent person with—*
> *(a) 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, and*
> *(b) the general knowledge, skill and experience that the director has.*

Evidently, as the High Court rightly observed in**Gregson vs. HAE Trustee Ltd and Others**,[159] s.174 merely codified existing dicta from the previous case law discussed above.The law has thereby effectively classified directors so that 2(a) takes into consideration the particular responsibilities attached to the office of any particular

[157]Finch, V. op.cit.at p. 201.
[158]Per Lord Goldsmith of the Lords Grand Committee at the Committee hearing on 6 February, 2006. See Hansard, Column 284. *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007), p. 12, accessible at http://www.berr.gov.uk/files/file40139.pdf.
[159](2008) EWHC 1006.

director—for example, a director of sales in a computer software company. It is by the general standard of this class of directors that he is to be judged, so that the director's conduct should be appropriate for the particular position that he occupies. Further, if he happens to have special qualifications beyond those required under the general standards, 2(b) holds him to those extra qualifications—for example, if the director of sales happens also to be a computer programmer. It is therefore, a cumulative requirement.[160] In effect, a director having a lot of knowledge and experience would be expected to use it. Apparently, the difference between s. 174 and the earlier common law decisions is that in the latter, the director's subjective level of skill sets the standard required of the director, whereas under s. 174, the director's subjective level does so only if it improves upon the objective standard of the reasonable director.[161]

The Act clearly does not distinguish between executive and non-executive directors with regard to the duties here discussed. However, although subject to a uniform and objective duty of care, what the discharge of that duty requires in particular situations will not necessarily be uniform for executives and non-executives alike, nor, for that matter, between different types of executive directors or even different types and sizes of companies.[162] This fact is evident from s.174 in stating that what the law would expect from the director would all depend on "the functions carried out by the director in relation to the company." Therefore, objective/subjective standard is also significant for non-executive directors because they would first be subjected to the standards of non-executives generally and then, if they happen to have any special knowledge or skills, to those subjective criteria. Thus, even non-executive directors may

[160]Per Lord Goldsmith of the Lords Grand Committee at the Committee hearing on 6 February, 2006. See Hansard, Column 284. *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007), p. 12, accessible at http://www.berr.gov.uk/files/file40139.pdf.
[161]Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 520.
[162] Ibid.

be subjected to higher standards than some executive directors, if the former happen to have some special qualifications.

A recent case which considered s. 174 is **Abbey Forwarding Limited (in liquidation) vs. Hone**,[163] wherein the English High Court observed that in deciding whether directors have fallen short of their duty of skill and care, particularly where the breach of duty concerned the precise way in which the business was run, evidence of what was normal in the field of commerce in which the company operates is of considerable relevance. The court then ruled that, taking various factors together, and in the absence of evidence about industry practice, it was not prepared to find the directors were in breach of their duty of skill and care to the company. Clearly, therefore, every case will be decided based on the relevant circumstances.

Of course "reasonable" is a highly nebulous term. It still remains to be seen how the courts would actually interpret "reasonably diligent person" as well as the things that may "reasonably be expected of persons" carrying out the functions of a director in relation to this duty. It is important for the courts to clearly interpret these terms because the benchmark which s. 174 attempts to set, is actually implicit in them.[164] Importantly, the imposition of an objective standard does not necessarily require a directorship to be regarded as a profession, since the courts would presumably define "what is reasonable" in relation to the director having regard to the knowledge, skill and experience which a person in his position ought to have.[165] Even non-executives would be required to measure up to some reasonable standard in carrying out their duties of guiding and monitoring the management of the company. A caution has been sounded, though, that

[163](2010) EWHC 2029 (Ch).cited in Bills Committee on Companies Bill: Follow-up to the Meetings on 3 and 10 June 2011 Supplementary Information (June 22, 2011). Financial Services and the treasury Bureau, Companies Registry, p. 8.Retrieved December 11, 2013, from http://www.legco.gov.hk/yr10-11/english/bc/bc03/papers/bc030628cb1-2577-1-e.pdf.
[164]Davies, J. (2007).Op.cit., at p.42.
[165]Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 520.

the courts cannot afford to be too hard on directors in their interpretation of reasonableness, considering the complexities of modern companies where many transactions are carried out simultaneously in dispersed geographical locations, or they would make it difficult for boards to find directors.[166] Besides, the courts would not want to end up being made into assessors of business risk, a role for which they are obviously unsuited.[167]

Interestingly, the demand for higher standards for directors in the discharge of their duties,resulted in the current practice whereby directors obtain insurance against their potential liability for negligence.[168] Indeed, s. 233 allows a company to purchase and maintain insurance for its director against liability arising from negligence and others. It is generally conceded that companies essentially take risks and so even where directors act in good faith while displaying the relevant care and skill, the result may still be disastrous. Thus, the fact that a company makes a loss, or even fails totally, is not necessarily indicative that its directors have been negligent in the management of the company's affairs.[169] And since the law does not allow the company to relieve the director from the duty under s. 174,[170] it is submitted that in allowing the company to take out an insurance policy for its director, the law has thereby aided it in circumventing the law by insuring the director against whatever amount he may be asked to pay. Supposedly, the idea is that, in this manner, companies shield directors who make loss-generating decisions reasonably after collecting all the appropriate evidence and after appropriate consultation and evaluation. But it is argued, and this

[166]Pettet, B. Op.cit.
[167]Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 523.
[168]Pettet, B. Op.cit.
[169]Worthington, S. op.cit.at p. 10.
[170]Although curiously, s. 1157 empowers the court to excuse directors for breach of duties committed under reasonable circumstances. Hoffmann LJ. Expressed doubts, in *Re D'Jan of London Ltd* (1994) 1 BCLC 561 that a person found to have been guilty of negligence, which involves failing to take reasonable care, can ever satisfy a court that he acted reasonably. It means that conduct may be "reasonable" for the purposes of s.1157 despite amounting to lack of reasonable care at common law.

writer quite agrees, that fully insured directors may have little financial interest in taking care, particularly if they do not pay their own premiums.[171]

In some jurisdictions,[172] this issue is effectively taken care of by the business judgment rule which is designed to accommodate such careful, yet unlucky directors. It has been suggested that there is no need for the equivalent of the business judgment rule in the Act, as the normal rules of negligence already accommodate instances covered by that rule.[173] Besides, even the business judgement rule is a protection available only to competent directors.[174] Usually, where a director is able to prove circumstances exonerating him from liability, he would not be found liable.

It is pertinent to note that although s. 174 clearly refutes some of the conclusions reached by Romer J. above, the part as to delegation, to a certain extent, remains an extant principle of UK corporate law.[175] In other words, the permission to delegate is still available to the director, although he must monitor the delegate reasonably to ensure the proper discharge of the responsibilities. In **Re Barings Plc.**,[176] the court clarified that the fact that a director is allowed to delegate "does not absolve a director from the duty to supervise the discharge of the delegated functions."[177] However, when once the director discharges this duty to the best of his ability, while being confident of the person he has put in charge, he cannot be liable for the negligence or fraud of that delegate or employee. In any case, his liability would all depend on the circumstances.[178]

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[171]Finch, V. op.cit.at p. 212.
[172]Notably, the United States and Australia.
[173]The Law Commission and the Scottish Law Commission.*Company Directors: Regulating Conflicts of Interest and Formulating a Statement of Duties*, Cm. 4436, 1999, Pt. 5; Worthington, S. op.cit, p. 10.
[174]Finch, V. op.cit.at p. 189.
[175] Especially considering s. 170(3) and (4) acknowledges the continued application of common law principles presumably not in conflict with the Act.
[176] (No. 5) (2000) 1 B.C.L.C. 433.
[177]Per Jonathan Parker J. ibid. at p. 489.
[178]See *Lexi Holdings Plc vs. Luqman* (2009) EWCA Civ 117.

The duty under s. 174 is particularly important because of the Company Directors Disqualification Act 1986 and the Insolvency Act 2000, which combine to generally disqualify certain persons in certain situations from being involved in the formation or management of companies and, in particular, from being company directors in the future.[179] Any director found liable for the breach of the duty under s. 174 can, as a result, be disqualified for a period ranging from 2 to 15 years, from holding directorship positions.[180] This is apart from the publication of his name in a register maintained by the Secretary of State, which effectively puts him on a notional "red list" so that companies and the public may take note.

It has been opined that the view that more qualified persons are subjected to higher standards of duty, is counter-productive in the long term, as it may deter such able, qualified persons from opting for the office.[181] It is here submitted that this may not be the case. Such directors can effectively retaliate by raising their "prices" or contract with the company to take out insurance policies on their behalf. Conversely, directors owe it to their company—indeed, it is in harmony with the expectation of good faith on their part—to afford the company any and all special qualifications they have, especially if this was the basis upon which the company hired them in the first place. Obviously, the new regime proposed by the tenor of s. 174 requires prospective directors to be alert to their future responsibilities. A director cannot complain that the standards required of him by s. 174 are unfair. He does have a choice whether or not to accept directorial responsibility, after considering his qualifications and the level of

[179] See ss. 6 and 11 of the Company Directors Disqualification Act.

[180] Such a disqualification order was made in relation to some senior executive directors following the collapse of Barings Bank. See *Baker vs. Secretary of State for Trade and Industry* (2001) BCC 273.

[181] Roach, L. op.cit., at p. 3. According to this author, "it is surely a better state of affairs to attract qualified, educated professionals and risk a minority of them not bringing their expertise to bear, than to deter such people to such an extent that our boardrooms are devoid of solicitors, accountants and other professionals." A similar worry was expressed by Lockhart J. in *Australian Innovation Ltd. vs. Paul Andre Petrovsky* (1996) 14 ACLC 1357.

commitment he knows he is prepared to put in. The English court has observed, rightly in this writer's view, that

> *Anyone accepting the office of director was required to understand the nature of the duty which he/she was called upon to perform. The nature of that duty would depend on the size and business of that company and the experience the director held himself out as having.*[182]

It would seem, therefore, that the practice whereby prospective directors embellish their resumes in order to impress companies hiring them, will be greatly discouraged. After all, no director would want to be held to standards he is in fact incompetent to justify, considering the consequences.

4.2.6 Duty to Avoid Conflicts of Interest

Directors are the mind and limbs of the corporation.[183] But they are also the mind and limbs of their individual, natural selves. Clearly, when two "bodies" are controlled by one mind, there is bound to be a clash of interests. The director's office is a fiduciary one: the law expects the director to act always in good faith for the utmost benefit of his *cestuique trust*, the company. While discharging his duties, the director is only to look to the interests of that entity and keep his own interests aside. Accordingly, s.175(1) states that "a director of a company must avoid a situation in which he has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company." In other words, he must look to avoiding any conflict of interests. But where there is a clash—and the law realises that the director being human, there often will be[184]—there are rules that must be observed.

[182] *Re Barings Plc*. (No. 5) (2000) 1 B.C.L.C. 523.
[183] *Bolton (Engineering) Co. Ltd. vs. Graham & Sons* (1957) 1 QB 159.
[184] Consider Lord Herschell's remark in *Bray vs. Ford* (1896) A.C. 44, HL, 51-52, quoted infra.

The rule that the fiduciary must avoid conflicts of interest generally has two consequences in equity.[185]In the first place, the fiduciary must prevent any possibility that there has been a conflict of interest.[186]Secondly, the fiduciary will also be required to account for—or disgorge—any unauthorised profit acquired as a result of a conflict of interest.[187]These equitable principles are sometimes broadly referred to as the 'no-conflict/no-profit rule' and include rules as to disclosure regarding self-dealing transactions[188] as well as prohibition of bribes and other secret profit.[189]

The earliest decision of the House of Lords reported on the point of conflicts between the interests of fiduciaries and their duties to their beneficiaries, is **Keech vs. Sandford**,[190] which held that a fiduciary may not take unauthorized profits from his office.The courts have sinceconsidered this core principle of equity[191]and pillar of fiduciary law[192]as also extending to the company director so that he is under strict obligation to avoid any conflict situations arising between his fiduciary duties to the company and his own personal interests. This may manifest where, for example, the director of Company A becomes a majority shareholder in Company B and Company B happens to be a supplier to Company A, or the director of Company A personally decides to bid for the same contract for which Company A is also bidding. Where a situation of multiple directorships arises, the rule becomes clearer, especially where the companies are engaged in the same line of business. Here, the director who happens to

[185] Hudson, A. op.cit., p. 25.
[186] See their Lordships of the House of Lords dicta on the point in *Aberdeen Railway Co vs. Blaikie Bros* (1854) 1 Macq 461, 471, [1843-60] All ER Rep 249, 252, *per* Lord Cranworth; *Bray vs. Ford* [1896] AC 44, at 51; [1895-99] All ER Rep 1009, at 1011, *per* Lord Herschell; *Regal vs. Gulliver* [1942] 1 All ER 378; *Boardman vs. Phipps* [1967] 2 AC 47. This principle is now codified under s.175(1).
[187]*Regal vs. Gulliver* [1942] 1 All ER 378; *Boardman vs. Phipps* [1967] 2 AC 47; CMS Dolphin Ltd. vs. Simonet (2001) 2 BCLC 704; *Sinclair Investment Holdings SA vs. Versailles Trade Finance Ltd.* (N0.3) (2007) EWHC 915, 10 ITELR 58.
[188]Expressly excluded from the purview of s. 175 by s. 175(3).
[189] All discussed separately in succeeding sub-headings in this work.
[190] (1726) 2 Eq. Cas. Abr. 741.
[191] Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 560; Hudson, A. op.cit.at p.25.
[192]Christie, M. (1992). The Director's Fiduciary Duty Not to Compete. *Modern Law Review,* 55(4): 506-520, at 507.

hold offices in both companies will find that he owes each a separate duty to avoid any conflicts between his duties to the company and any 'outside' duty he may owe others.[193]

To be sure, self-dealing transactions as well as the obtaining of secret benefits, are also manifestations of conflict situations which are prohibited under the law. But these two aspects of the broader no-conflict rule are not contemplated by s.175, having been addressed separately under subsequent sections.[194] However, the prohibition in all cases, even before the codification of the law in the Act, has always been strict. The only exception is where the director had made a disclosure of his personal interest or the secret profit to the company in general meeting, and his pursuance of it had been sanctioned accordingly, or unless he was protected by an appropriately worded provision of the articles.[195]

Even though the Act does not state anywhere that the director is a trustee with regards to the company, clearly, the law regards the company director as a trustee of the company's property, information, and opportunity. Accordingly, s. 175(1) provides that "a director of a company must avoid a situation in which he has, or can have, a direct or indirect interest[196] that conflicts, or possibly may conflict, with the interests of the company." What can be regarded as "interests" in relation to the company in this context has not been defined. However, the next subsection helpfully provides: "this applies in particular to the exploitation of any property, information or opportunity..." In other words, these belong to the company and therefore, only the company is rightfully entitled to enjoy them, especially considering the fact that they are available to the

[193] *Transvaal Lands Co. vs. New Belgium (Transvaal) Land and Development Co.* (1914) 2 Ch. 488 (CA).S.175(7) now codifies this principle.
[194] In fact, s.175(3) expressly removes self-dealing transactions from the ambit of s.175.
[195] *Aberdeen Rly.Co. vs. Blaikie Bros* (1854) 1 Macq. 461. See further Birds, J. et al. op.cit. at p. 647.
[196] A good example of an indirect interest could be where a director represents a major shareholder in the company whose interests conflict with those of the company.

director only by virtue of the office he holds in the company.[197] The uncompromising application of this principle has sometimes been questioned.[198] Yet, the courts have from the onset maintained that the principle is as it should be. Lord King once attempted a defence:

> *This may seem hard, that the trustee is the only person of all mankind who might not have [the property]: but it is very proper that rule should be strictly pursued, and not in the least relaxed; for it is very obvious what would be the consequence of letting trustees have the [property]…"*[199]

Thus, the rule is often applied strictly,[200]so that no defence was furnished by establishing,[201] for example, that the director acted honestly and in good faith throughout;[202] that the profit was acquired through the use of the director's own property and/or skill as well as through his directorship;[203] that the disclosure to the general meeting would have been a mere formality because at a general meeting the director had or could have summoned sufficient votes to pass a resolution approving his retention of the profit;[204] or that none of the shareholders at the time of the proceedings for an account was a shareholder at the time when the profit was made.[205]

The idea is that investors having advanced their money and placed their trusts in the management of the company, are entitled to some assurance that the company's

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[197]*Green & Clara Pty. Ltd. vs. Bestobell Industries Pty. Ltd.* (1982) WAR 1, at 5-6.

[198] For example, there have been criticisms of its application in *Regal (Hastings) Ltd. vs. Gulliver* (1942) 1 All ER 378. See Wild, C. and Weinstein, S.op.cit. at 335; Davies, L.P. and Worthington, S. op.cit. at 593; Birds, J. et al. op.cit. at pp. 647-648.

[199]*Keech vs. Sandford* (1726) Sen. Cas. Ch. 61.

[200] Hudson, A. op.cit., p. 32; Corkery, F.J. (1987).*Directors' Powers and Duties*, Longman Cheshire, Melbourne Australia, p. 83; Christie, M. op.cit., at p. 509. See also the cases of *Regal (Hastings) Ltd. vs. Gulliver* (1942) 1 All ER 378;*Boardman vs. Phipps* [1967] 2 AC 47 and *Keech vs. Sandford* (1726) Sel. Cas. Ch. 61.

[201] See Birds, J. et al. op.cit. at pp. 648-649.

[202]*Parker vs. McKenna* (1874) 10 Ch App 96; *Costa Rica Ry Co. vs. Forwood* (1901) 1 Ch 746; Boardman vs. Phipps (1967) 2 AC 46, HL.

[203]*Parker vs. McKenna* (1874) 10 Ch App 96; *Regal (Hastings) Ltd. vs. Gulliver* (1942) 1 All ER 378; *Industrial Development Consultants vs. Cooley* (1972) 2 All ER 162.

[204]*Regal (Hastings) Ltd. vs. Gulliver*, supra.

[205]As was the case in *Regal (Hastings) Ltd. vs. Gulliver,* supra.

assets and other benefits are applied only to the company's activities and exclusively for it and that the directors advert their minds as well as skills only to the company's advancement, and not their own personal profit. Thus, the reason for this principle of law is evident. The company ought to be a beneficiary of directors' fiduciary duties, yet affords directors great powers, and is thereby exposed to boardroom mischief.[206] These powers are reinforced when some or most of the directors also happen to be major shareholders of the company as well.[207] Where this is the case, the law particularly reinforces the status of the company as a single personality, distinct and separate from all those associated with it. The directors would even then be required to still set aside their own interests as members and instead, satisfy the interests of "the company." Lord Herschell once remarked that

> *A person in a fiduciary position...is not, unless otherwise expressly provided... entitled to make a profit... It does not appear to me that this rule is, as has been said, founded upon principles of morality. I regard it rather as based on the consideration that, human nature being what it is, there is a danger, in such circumstances, of the person holding a fiduciary position being swayed by interest rather than by duty, and thus, prejudicing those he was bound to protect. It has, therefore, been deemed expedient to lay down this positive rule.*[208]

Along these lines, Wooten J. of the Australian Supreme Court once adopted the controversial position that

> *Courts will not burden themselves with the difficult and multitudinous enquiries as to whether a person in a fiduciary position has, in all the circumstances, succumbed to temptation. They simply insist that such a person does not act in a way in which he is exposed to temptation.*[209]

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[206] Corkery, F.J. op.cit.p. 77.
[207] As was the case in *Regal (Hastings) Ltd. vs. Gulliver* (1942) 1 All ER 378, discussed infra.
[208] *Bray vs. Ford* (1896) A.C. 44, HL, 51-2.
[209] *Queensland Mines Ltd. vs. Hudson*[1976] ACLC 28,658 at 28,685.

But the Privy Council rejected this viewpoint on appeal, stating that there always had to be a real, sensible possibility of conflict of interest. As provided in s. 175(1), and observed by Lord Upjohn,[210] this rule applies where there is an *actual* as well as *possible*, conflict situation. Thus, unlike the common law, the main idea in s.175 is a duty to avoid possible conflict of interest situations, rather than duty to refrain from benefitting from them.[211] However, the question whether an actual or potential conflict of interest has arisen, is one for the courts.[212]In **Boardman vs. Phipps**[213]it was held that the term 'possibly may conflict' means 'that the reasonable man looking at the relevant facts and circumstances of the particular case would think that there was a *real sensible possibility* of conflict. The test is therefore one of 'reasonability'.

Further, s. 175(4)(a) confirms, as suggested by case-law,[214] that there is a situation of conflict only where that can *reasonably be regarded as likely to arise*.[215] Thus, for example, where a non executive director of a company in a business focussed upon the provision of loans, mortgages and financial advice, is offered a position in a company involved in food processing, the situation cannot reasonably be regarded as *likely to give rise to a conflict* of interest, nor even of duties.[216] Lord Goldsmith has

[210]*Boardman vs. Phipps* [1967] 2 AC 47.
[211]Hudson, A. op.cit., at p.26.
[212] Davies, P. and Worthington, S. (2012). Op.cit. at 591.
[213](1967) 2 AC 46
[214]Such as *Bhullar vs. Bhullar* (2003) EWCA Civ. 424; (2003) 2 BCLC 241.
[215] The government believes that this introduces the concept of "reasonableness" which makes the situation easier from the point of view of a director and avoids a very harsh test, although it is still a heavy duty and intended to be so. See *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 12, quoting Lord Goldsmith of the Lords Grand Committee from the Hansard of February 6, 2006, column 293, accessible at http://www.berr.gov.uk/files/file40139.pdf.
[216] However, in *Allied Business and Financial Consultants Ltd. vs. Shanahan* (also known as *O'Donnell vs. Shanahan*) (2008) EWHC 1973 (Ch), which decision was overturned in 2009, the appeal court took the view that where a company's business was not restricted by its constitution, it was fully open to it to engage in any kind of business. In *Bhullar vs. Bhullar* (2003) 2 B.C.L.C. 241, C.A. as well, the court allowed the company stake a claim on an opportunity in a line of business it had, albeit informally, previously decided not to continue. These views have been criticised as having the potential to "raise the risks for directors and increase the chances of pure windfall gains to the company and its shareholders," since a director would then be bound to present *every* entrepreneurial idea to the board before pursuing it individually. SeeDavies, P. and Worthington, S. (2012).Op.cit. at 601.

clarified that if the matter fell outside the ambit of the company's business, a real conflict of interest is *unlikely*.[217] But where, for example, a director of a fishing company at the same time sets up and runs another company engaged in seafood processing, this situation of 'interlocking directorships' may reasonably be regarded as likely to give rise to both a conflict of interest as well as duties, since the director would, quite clearly, seem to be 'competing with the company.'

Generally, serving on the boards of two competing companies has been frowned at.[218] At least, Louis Brandeis, a one-time justice of the U.S. Supreme court, certainly condemned the practice in very strong terms thus:

> *The practice of interlocking directorates is the root of many evils. It offends laws human and divine. Applied to rival corporations, it tends to the suppression of competition . . . Applied to corporations which deal with each other, it tends to disloyalty and to violation of the fundamental law that no man can serve two masters. In either event, it tends to inefficiency; for it removes incentive and destroys soundness of judgment.*[219]

However, for a long time, dicta in decisions such as **London &Mashonaland Exploration Co. vs. New Mashonaland Exploration Co**[220] and **Bell vs. Lever Bros**[221] gave the oft-disputed impression[222] that competing directorships were not automatically a breach of fiduciary duties.[223] But the more recent decisions in **In Plus Group Ltd. vs.**

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[217] Lord Goldsmith of the Lords Grand Committee, reported in the Hansard of May 9, 2006, column 864. Cited in: *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 13, per, accessible at http://www.berr.gov.uk/files/file40139.pdf.

[218] *Bristol and West Building Society vs. Mothew*[1998] Ch 1 18, CA.

[219] Breaking the Money Trusts.*Harper's Weekly.* December 6, 1913, at p. 13, quoted in Seplaki L. (1982). *Antitrust and the Economics of the Market.*Harcourt,New York,p. 594. Cited in Christie, M., op.cit.atp. 506.

[220] (1891) WN 165.

[221] (1932) A.C. 161. The decision here is that a director is not accountable for the profits of a competing business which he may be running, unless the articles or his service contract expressly provide so.

[222] See Davies, P. and Worthington, S. (2012).Op.cit. at 606 and Christie, M. op.cit., at p. 506.

[223] Although competing trust executors apparently were. See *Re Thomson* (1930) 1 Ch. 203. Some have questioned why this should be so, considering the job of a director and that of a trustee require almost

Pyke[224] and **Foster Bryant Surveying Ltd. vs. Bryant**[225] suggest that there is no standard rule on the point as each case is to be decided based on the facts.[226]However, the court now tends to take the view that a fiduciary who acts for two principals with potentially competing interests without the informed consent of both is in breach of the obligation of undivided loyalty as he thereby puts himself in a position where his duty to one *may* conflict with his duty to the other.[227]

Usually, the case of a director acting for competing companies arises in cases where the director forms a new company with the intention of resigning from the current company in order to go into the same line of business,[228] as was the situation in some cases discussed below. After resignation, the director is generally allowed to compete freely subject to any contractual restraints, the law relating to trade secrets and the rules relating to corporate opportunities acquired *before* resignation.[229]Thus, it was decided in **CMS Dolphin Ltd. vs. Simonet**[230]that where a director forms a company in order to exploit a maturing business opportunity of another company to whom he is a director, that company he forms is accountable for the profits properly attributable to the breach of duty. As for multiple directorships of non-competing companies, these usually pose no problem although the court has ruled that a director of two or more

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an equal degree of loyalty to the "trust". See for example Christie, M. op.cit., particularly at 512; and Sealey, L. (1967). The Director as Trustee.*Cambridge Law Journal*, 83 at 97.

[224](2002) EWCA Civ. 370; (2002) B.C.L.C. 201, CA. The majority of the Court of Appeal in this case supported the decision in *London and Mashonaland Exploration Co. vs. New Mashonaland Exploration Co. supra.*

[225](2007) EWCA Civ. 239; (2007) 2 All ER (Comm.) 285.

[226]As Lord Upjohn observed in*Boardman vs. Phipps* (1967) 2 A.C. 46 at 67, "Rules of equity have to be applied to such a great diversity of circumstances that they can be stated only in the most general terms and applied with particular attention to the exact circumstances of each case."

[227]*Bristol and West Building Society vs. Mothew*[1998] Ch 1 18, CA.

[228] Davies, P. and Worthington, S. (2012). Op.cit. at 607.

[229] Davies, P. and Worthington, S. (2012). Op.cit. at 608-609. In fact, it has been said that equity would condemn competitiononly where there has not been consent obtained by the director after full disclosure. See Christie, M. op.cit., at p. 506. It has also been decided that the director may not solicit the customers of his former employer. See *Aubanel and Alabaster Ltd. vs. Aubanel* (1949) 66 RPC 343 at 346; *Christie & Co. Ltd. vs. Greer* (1981) 4 WWR 34.

[230](2001) 2 B.C.L.C. 704.

companies generally takes the risk of a petition against him alleging unfair prejudice against members under s. 459 of the 1948 Act,[231] if he subordinates the interests of one company for those of the other.[232]

The no-conflict/no-profit rule, as provided in s. 175(2), applies equally to property, information and opportunity of the company.[233] Property in this context has been interpreted widely by the courts to include construction contracts,[234] patent rights,[235] any contracts and business opportunities that come to the director whilst he serves the company and which he ought to give the company the chance to acquire or acquire for the company[236] and even an invention by a director whilst he severs the company, if the invention is related to the company's business.[237] However, the bulk of cases often involve the exploitation of information and opportunity. The profiteer would only be called to account if the opportunity, etc. in question can be reasonably attributed to the company, but it matters not that the knowledge of the opportunity came to the director whilst he was acting in his individual capacity, as long as it is related to the company's business.[238] The fundamental question, therefore, is: when can it be said that an (economic) opportunity exploited by a director rightfully belongs to the company he serves in order to entitle the company to any profits made? There are clues provided within s.175 itself:

1. the opportunity, etc. is an "interest" of the company (s.175(1));
2. the director's interest may be "direct or indirect" and mere *possibility* of conflict is enough (s.175(1));
3. in any case, it is immaterial whether the company could actually take advantage of the opportunity, etc. (s.175(2));

[231] Now s. 994
[232] *Scottish Co-operative Wholesale Society Ltd. vs. Meyer* (1958) 3 All ER 66.
[233] In truth, all three are, collectively, the "property" of the company.
[234] See *Cook vs. Deeks* supra.
[235] *Cranleigh Precision Engineering Ltd. vs. Bryant* (1965)1 WLR 1293.
[236] *Canada Safeway Ltd. vs. Thompson* (1951) 3 DLR 295.
[237] *British Syphon Co. Ltd. vs. Homewood* (1956) 1 WLR 1190.
[238] This conclusion can be drawn from cases such as *Regal (Hastings) Ltd. vs. Gulliver* (1967) 2 A.C. 134 and *Peso Silver Mines Ltd. vs. Cropper* (1966) 58 DLR (2d.) 1.

4. self-dealing transactions are not contemplated here (s.175(3));
5. the situation must be reasonably regarded as likely to result in conflict of interest (s.175(4)(a));
6. exploitation of corporate opportunity, etc. is not prohibited where it is authorised (s.175(4)(b)).

Evidently, in spite of the pointers above, the question is still clearly unanswered, especially considering points 2 and 5 above appear to be conflicting. Helpfully, s. 170(4) & (5) point out that the duties codified under the Act are based on common law rules and equitable principles and are therefore, to be interpreted and applied in the same way. An examination of cases on the point[239] would reveal that some courts limit the doctrine to situations where the company is considered to have an "expectancy or inchoate interest" in the particular transaction.[240] Others extend it to all opportunities which fall within the company's line of business,[241] while a third variant is provided by those courts which reject these tests and determine liability by the application of what appear to be ethical standards of what is fair and equitable to particular sets of facts.[242] But in every case, the question of how substantial the "interest" has to be in order to qualify for prohibition, is one settled by the court.[243]

[239] Such a task was attempted by Prentice, though he based his observations mostly on American decisions. See Prentice, D.D. (1974).The Corporate Opportunity Doctrine.*Modern Law Review*. 37(4): 464-468, at p. 464.

[240]In *Lagarde vs. Anniston Lime and Stone Co.* (1900) 28 So. 199, 201, the court referred to "property wherein the corporation has an interest already existing or in which it has an expectancy growing out of an existing right..." Sometimes, it is also required that the company must also need the "opportunity" for its continued existence and prosperity. See *Solimine vs. Hollander* (1940) 16 A. 2d. 203, 215.

[241]Particularly U.S. courts. See *Rosenblum vs. Judson Engineering Corp*. (1954) 109 A. 2d. 558, 563, where the court observed that "the issue to be determined...is whether...(the opportunity) was so closely associated with the existing and prospective activities of the corporation that the defendants (the directors) should fairly have acquired that business for or made it available to the corporation."

[242]*Aas vs. Benham* (1891) 2 Ch. 244 at 255 and 260. Though based on partnership, the court likened the position of a partner in the firm with that of a director. See also *Durfee vs. Durfee and Canning Inc*. (1948) 80 N.E. 2d. 522, 529; *Island Export Finance Ltd. vs. Umunna* (1986) BCC 460 and the Privy Council decision in *Queensland Mines Ltd. vs. Hudson* (1978) 52 A.L.J.R. 379.

[243] For example, in *Todd vs. Robinson* (1884-1885) 14 QBD 739 and *Transvaal Lands Co. vs. New Belgium (Transvaal) Land and Dev. Co.* (1914) 2 Ch. 488 , the court suggested that the director's holding of a very small interest as shareholder of a company that is contracting with the director's company, is enough.

The case of **Regal (Hastings) Ltd. vs. Gulliver**[244] was certainly squared on corporate opportunity. Though previously discussed,[245] the rather interesting facts merit restatement here. The plaintiff company, which owned one cinema, was desirous of acquiring the leases to some other two through a subsidiary company it formed for that purpose. The intention was to eventually sell all three cinemas as a going concern. However, the lessor of the two new cinemas required the subsidiary to have a paid-up capital of £5000 (in lieu of a guarantee of the rent under the proposed lease), but the plaintiff could only afford 2000 of the 5000 £1 shares. To help find the extra capital, four of the five directors each bought 500 shares. The chairman of the board also caused his associates to buy another 500 shares, while the company's solicitor took up the remainder. Three weeks later, the sale of the three cinemas was indirectly carried out by the sale of the shares in the subsidiary, rather than by sale of the undertaking itself, at a profit of almost £3 per share. The new board of directors to the plaintiffthereafter proceeded against the former directors and the solicitor, seeking the profits they had made on the sale of their shares in the subsidiary.

Having come to the conclusion that "what the directors did was so related to the affairs of the company that it can properly be said to have been done in the course of their management and in utilisation of their opportunities and special knowledge as directors,"[246] the House of Lords easily found the directors liable. Although it was found as a fact that the directors acted throughout in good faith, they were still made to pay over their profits to the company as only a proper ratification of the transactions by the general meeting could have availed them. Unfortunately, this, they neglected to procure, even though this would have been easy since they controlled the majority of the plaintiff's sharesthroughout the relevant period. The equitable principle was strictly

[244](1967) 2 A.C. 134.
[245] See **3.7** supra.
[246]Per Lord Macmillan at p. 153.

applied, in spite of the fact that the company in fact could not have taken advantage of the opportunity due to lack of sufficient funds at the time.[247]

This decision has been criticized[248] for having taken equitable principles to inequitable conclusions,[249] not only because the chairman and solicitor who ought to take the most blame were exonerated from accounting,[250] nor even because the persons bringing the action sought, as it were, to reap where they did not sow, but also becausethe ruling suggested that the mere possession of information which results from the holding of office as a director is sufficient to raise the duty to account.Besides, the directors had not really deprived the company of any of its property, since the shares in the subsidiary were bought with their own money and those shares had never in fact been the company's property.[251] Yet, Lord Russell justified the decision of the court thus:

> *The rule of equity which insists on those who, by use of a fiduciary position, make a profit being liable to account for that profit, in no way depends on fraud, or absence of bona fides; or upon such questions or considerations as whether the profit would or should otherwise have gone to the plaintiff, or whether the profiteer was under a duty to obtain the source of the profit for the plaintiff, or whether he took a risk or acted as he did for the benefit of the plaintiff, or whether the plaintiff has in fact been damaged or benefited by his action. The liability arises from the mere fact of a profit having, in the stated circumstances, been made. The profiteer, however honest and well-intentioned, cannot escape the risk of being called upon to account.*[252]

[247] Perhaps in order to clarify the law here, s.175(2) states that "it is immaterial whether the company could take advantage of the property, information or opportunity.

[248]See Davies, P. and Worthington, S. (2012).Op.cit. at 593;Wild, C. and Weinstein, S.op.cit.at 335.

[249] Davies, P. and Worthington, S. (2012). Op.cit. at 594.

[250]Since the chairman did not take the shares as a beneficial owner but simply caused his associates to subscribe while the solicitor took at the express request of the board.

[251]Wild, C. and Weinstein, S.op.cit.at 335.

[252]*Regal (Hastings) Ltd. vs. Gulliver* supra, at 144-145.

Therefore, it cannot be overemphasized that the rule is strict. The nature of this fiduciary duty is such that it supersedes the relationship. For this reason, s.170(2) still holds a director to his duty under s.175, even after his resignation from office, as regards the exploitation of any property, information or opportunity of which he became aware at a time when he was a director. This is necessary in order to *nip* an otherwise obvious escape route *in the bud.* Indeed, as Prentice aptly remarked, "it would be fatuous to allow directors to immunise themselves against liability by resigning immediately prior to the acquisition of the opportunity."[253] There certainly abound cases in which such has been the case.[254]In **Industrial Dev. Consultants Ltd. vs. Cooley**,[255]the managing director did not tell his company that a project was going to be revived after the rejection by a gas board of his company's offer; nor did he disclose that he had been negotiating future employment with the gas board. In order to take the advantage of this renewed offer, he represented to the company that he was ill and thereby procured the termination of his employment on short notice. Shortly after, he successfully obtained the contract with the gas board. The defendant then sued for an account of the profits. Roskill J., after considering that the director had accepted employment with the gas board, doing the very work he had unsuccessfully tried to get for the plaintiff company and had also faked illness in order to gain quick release from his employment with the plaintiff, ruled that the director had been in breach and was therefore liable to account.

Similarly, in **Crown Dilmun vs. Sutton**,[256] a director learned of an opportunity to develop a football ground which he exploited on his own account once his contract of employment had been terminated. It was found that he had not made full disclosure to

[253]See Prentice, D.D. (1974).Op.cit. at p. 467.
[254]*Cook vs. Deeks*; *Industrial Dev. vs. Cooley*; are but a few.
[255](1972) 2 All ER 162.
[256](2004) 1 B.C.L.C. 468.

the claimant company of the extent of the opportunity. Consequently, he was liable to account to the claimant for the personal profits realised from the transaction.

It can be observed from the cases discussed above that an issue most central to the exploitation of corporate opportunity etc., is authorisation—and by implication, disclosure—which is one exception to the application of the principle of no-conflict. S. 175(4)(a) provides that the duty to avoid conflicts of interests is not infringed where the matter has been authorised by the directors. The authorisation regime introduced under s. 175 is one of the areas reviewed by the Companies Act from the former common law position. According to s.175(5)

> *Authorisation may be given by the directors—*
> *(a) where the company is a private company and nothing in the company's constitution invalidates such authorisation, by the matter being proposed to and authorised by the directors; or*
> *(b) where the company is a public company and its constitution includes provision enabling the directors to authorise the matter, by the matter being proposed to and authorised by them in accordance with the constitution*

Formerly, the common law did not condone authorisation of such situations by the board, insisting always on the general meeting as the proper body to act instead.[257] However, even the interested director, if he happened to be a shareholder, could participate in the authorisation process and vote.[258]But it was also decided in **Clemens vs. Clemens Bros Ltd.**,[259] that a director who also happened to be a majority shareholder, could not use her majority vote in general meeting "in whatever way she pleases", [for] that right [to vote] is "subject . . . to equitable considerations . . . which may make it unjust ... to exercise [it] in a particular way". Thus, fraud or inequitable

[257]*Benson vs. Heathorn* (1842) 1 Y. & C.C.C. 326; *Imperial Mercantile Credit Association vs. Coleman* (1871) L.R. 6 Ch. App. 558, C.A.; *Regal (Hastings) Ltd. vs. Gulliver* (1967) 2 A.C. 134.
[258] See *North-West Transportation Co. Ltd. vs. Beatty* (1887) 12 App. Cas 589; *Northern Counties Securities Ltd. vs. Jackson and Steeple Ltd*. (1974) 1 WLR 1133 at 1144, 1146; *Estmaco Ltd. vs. Greater London Council* (1982) 1 All ER 437 at 444.
[259](1976) 2 ALL ER 268 at 282.

conduct will not be permitted, regardless of the letter of the law. Apparently also, authorisation by the general meeting was not conclusive. It has been held that the majority of shareholders voting in general meeting are supreme only to the extent that "their acts are not inconsistent with the articles or otherwise *ultra vires* of the Company, and are not fraudulent ..."[260] In other words, if it was subsequently found out that the authorisation was a fraud or was not in the best interests of the company, it could be set aside.

However, due to changing business times,[261]and the general attitude of law against repression of entrepreneurship, a *softening* of the rule has been observed in case law, at least, within the commonwealth, especially in instances where the company can be said to have indirectly authorised the conflict, by a bona fide rejection of the opportunity in the first place. The first of such cases notable for admitting this is **Peso Silver Mines Ltd. vs. Cropper**[262] decided by the Supreme Court of Canada. In that case, the respondent was instrumental in incorporating a companyin 1959 which, two years later, transferred its assets to the appellant, Peso, a company in the formation of which the respondent also played a major role. Subsequent to this the appellant company went public but experienced strains on its finances. During 1962 an offer was made to the appellant to purchase mining claims, some of which were contiguous to claims already owned by the appellant. The then board of directors of the appellant company rejected this offer and the trial judge found this decision was made "in the best of faith and solely in the interest of the appellant, and not from any personal or ulterior motive on the part of any director, including the respondent." The major reason given for rejecting the offer was financial inability. Subsequent to this the respondent, in conjunction with two other directors and the company geologist, formed a company to

[260]Per Lord Wark in *Harris vs. A. Harris Ltd*. (1936) SC 183 at 191.
[261]Corkery, F.J. op.cit.at p. 85.
[262](1966) 58 DLR (2d.) 1.

purchase and exploit the claims. In 1963 the appellant, needing fresh supplies of capital, sold 1,000,000 shares to Charter Oil Co. Ltd. As a result control of Peso was transferred to the latter company. Representatives of Charter then requested the respondent to hand over his interest in the company formed to exploit the claims rejected by the appellant. The respondent declined to do thisand was dismissed for his contumacy. The Supreme Court upheld the judgment of the Court of Appeal dismissing the appellant's action and asserting that the respondent did not hold the shares in the company formed to exploit the above claims, in trust for Peso.

The court may have viewed the rejection of the opportunity by Peso above either as removing the conflict of interest problem and operating in the same way as disclosure does with respect to directors' contracts with the company, oras being tantamount to condonation or authorisation of the directors' conduct.[263] Some have questioned why the court should decide in this manner, especially considering the fact that the decision to reject the opportunity by the board had the dual characteristic of not only depriving the company of the business opportunity, but also of facilitating its subsequent exploitation by the directors, the very persons who made the decision to reject on behalf of the company.[264] One commentator went as far as to urge the English court not to adopt a similar stance on the issue, if it ever had to consider a similar situation.[265] But it did.

In **Queensland Mines Ltd. vs. Hudson**[266] the defendant had been managing director of the plaintiff mining company, where he learned of some potentially profitable mining contracts. The board of directors of the company decided not to pursue these opportunities after they had had all of the relevant facts explained to them, even in the

[263]Prentice, D.D. (1967). Regal (Hastings) Ltd. vs. Gulliver: The Canadian Experience. *Modern Law Review*, 30: 450-455, at p. 453.
[264]Davies, L.P. and Worthington, S. (2012).Op.cit. at pp. 598-599; Prentice, D.D. (1967).Op.cit., at p. 454; Corkery, F.J. Op.cit. at pp.92-93.
[265]Prentice, D.D. (1967).Op.cit., at p. 455.
[266](1977) 18 ALR 1.

knowledge that the managing director intended to do so on his own account. The defendant then resigned and pursued the business possibilities offered by the contracts on his own account, taking great personal risk in so doing. When he made profits from the opportunity however, the company sought to recover the profits generated. But the apex court held that the repudiation of the contracts by the company meant that the director was entitled to pursue them on his own account without a conflict with his fiduciary responsibility to the company, even though the opportunity had come to his attention originally by means of the fiduciary office.

In effect, the Privy Council here appeared to accept a board decision as releasing the corporate interest in an opportunity, just like the Canadian Supreme Court in **Peso** above. The reason given for this decision by the apex court was that the board, "fully informed as to all relevant facts, had reached a firm decision to renounce all interest in the exploitation of the licence and had assented to Mr Hudson taking over the venture for his own account".[267] Thereafter, there could not have been any sensible possibility of conflict of interest, even though the opportunity had come to Mr Hudson's attention originally by virtue of the office he held previously.

It has been suggested[268] that this rather surprising outlook of the courts in the two cases above may have been a bid to make the rule against conflicts more appropriate with "modern commercial reality." That is to say, it is considered a stifling of enterprise and impediment to free competition, particularly in a capitalist economy, to keep directors—especially former directors—bound by their loyalty to the company regarding opportunities already rejected by their companieswhere the rejection was bona fide. Yet, the fundamental question remains how can the courts be absolutely certain that the rejection of the opportunity was bona fide in the first place, considering it is the

[267] Ibid., at 8.
[268] See Corkery, op.cit. p.85.

directors' duty to secure the interests of the company? A fortiori, the directors would not be encouraged to do their best to secure the company's interests,[269] and, as Corkery puts it, "if a director stands to gain from the rejection of the opportunity, a shadow lies over the board's decision to reject."[270]It is further argued that impediments to a company exploiting any business opportunity, such as financial inability, the doctrine of *ultra vires*, or a specific decision to reject the opportunity, are surmountable hurdles and so, any director who makes use of the business opportunity in the above circumstances should still be made to account.[271]

In the more recent decision in **Foster vs. Bryant**,[272] the defendant director of the company was effectively forced to resign by his co-director, the majority shareholder, who excluded him from the company's operations. Before the defendant's resignation came into effect—while he was still technically a director but after he had tendered his resignation— one of the company's principal clients, who wanted to retain the services of the director, began to talk to the defendant about the way in which the defendant could work with this client. When the defendant's resignation took effect, he began to work for the client. The company sued the defendant on the basis that he had been a director when the business opportunity came to light and therefore any profits earned from that opportunity should be subject to an account in favour of the company. But Rix LJ sought to distinguish this case fromearlier decided cases on the rule against conflicts, concluding that the position changed in this company after the defendant's resignation such that he was excluded from the business and thus had only to act honestly in his role as director, and therefore, he was not required to account for his subsequent profits. Therefore, the principle against conflicts must be applied in a "fact-sensitive" way.

[269] See *Industrial Development Consultants vs. Cooley* (1972) 2 All ER 162, particularly at 176 and also *Irving Trust Co. vs. Deutsche* (1934) 73 F 2d. 121, 124 of the American court.
[270]Corkery, F.J. op.cit.at p.93.
[271]Prentice, D.D. (1967).Op.cit., at p. 454.
[272] (2007) Bus LR 1565.

The CLRSG may have been persuaded by court decisions such as those mentioned above, that show a softening of the rule, for it recommended making authorisation easier for interested directors. The group considered the previous framework regarding personal exploitation of corporate opportunities impractical, due to requirement for member approval in all cases, so that the framework was said to be "unduly strict" and "inconsistent with the principle that it is for the board to make business assessments and stifles entrepreneurship."[273] It therefore proposed, and Parliament accepted, that statute should allow the company's rights to be waived by a disinterested board.[274]In fact, the idea behind the content of s.175 is actually to *allow* conflicts, provided there is disclosure and authorisation.[275] Thus, changes were made in order to facilitate the exploitation of corporate opportunities "which might otherwise be left to waste because of the expense of convening a general meeting."[276]

Consequently, the Companies Act now allows disinterested or non-conflicted boards of private companies to consider proposals on such conflicts and decide whether or not to authorise them, provided there are no provisions within the articles inconsistent with this board power. As for public companies, the articles have to be explicit that the board does have the power to consider and authorise any such conflicts. In other words, the articles of public companies have to contain such a provision in order for the board to have the power to act in that manner. It is also interesting to note that not only is the authorising board required to be "disinterested", but each of its members, while authorising, is still held to his responsibilities of acting in good faith in the way he

[273] Company Law Review Steering Group, *Modern Company Law for a Competitive Economy: The Final Report*, Volume 1, London, DTI, 2001, p. 46
[274] Refer to s.175(5)(a)&(b) and (6)(a)&(b).
[275]Per Lord Goldsmith of the Lords Grand Committee.*Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 11, quoting from the Committee Report in the Hansard of 6th February 2006, column 288.Retrieved December 23rd 2013, from http://www.berr.gov.uk/files/file40139.pdf.
[276]Arden, D.B.E. op.cit, at 169.

considers that authorisation is the course of action most likely to promote the success of the company.[277] In either type of companies, where the shareholders wish to retain the power of authorisation, the articles can be drafted to reflect that preference. Where there are no disinterested directors left on the board, the Act is silent. Presumably, the matter would then have to be decided by the general meeting as per common law.[278] However, where the company's articles contain provisions for dealing with conflicts of interests, directors will not be in breach of duty if they act in accordance with those provisions.[279]

There seem to be other 'escape routes' for the 'conflicting director' under the Act, besides the disclosure and authorisation procedures set out in s. 175. S.1157 allows the court to wholly or partially excuse directors for breach of duty—including duty to avoid conflict of interest—on reasonable grounds. Though discretionary, this power of the court is exercised having regard to the circumstances of the case and in all cases, the good faith of the director. In **Coleman Taymar Ltd vs. Oakes,**[280]the plaintiff company was giving up business in the UK, and it was clear to the defendant that his role as director and employee was coming to an end. He therefore negotiated to take over leases that the company was giving up, with a view to setting up in the same line of business, recruited some of the company's staff, and canvassed the customers of the company, without seeking and obtaining permission. When he was sued by the company, the court held that preliminary activity short of active competition was

[277]Per Lord Goldsmith of the Lords Grand Committee.Quoted in *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 11, quoting from the Committee's Report in the Hansard of February 9 2006, column 327.Retrieved December 23rd 2013, from http://www.berr.gov.uk/files/file40139.pdf.

[278]S.180(4) preserves the common law rule as to authorization by the company. Since the Act does not explicitly prohibit interested members from voting on authorization, the assumption is that a conflicted director, if he happens also to be a member, is entitled to vote on the authorization of the conflict. Cf. the rule on ratification under s.239.

[279]Per Lord Sainsbury of Turville of the House of Lords.Quoted in *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 11, quoting from the Lords Report in the Hansard of 23rd May 2006, column 722.Retrieved December 23rd 2013, from http://www.berr.gov.uk/files/file40139.pdf. This is reflected in s.180(4)(b).

[280](2001) 2 BCLC 749.

permissible, but that his actions went beyond preliminary activity. The court awarded his former company £2 damages for breach of his contract of employment, with an inquiry as to any benefit that might have accrued to the director from his activities, but applied s.727 of the Companies Act 1985 (now s.1157) to excuse any breach of directors' duties.

Further, s.239 allows the ratification by a company of conduct by a directoramounting to negligence, default, breach of duty or breach of trust in relationto the company.[281] This would also cover any conflicts of interest situations. However, the resolution must be made by the members and, although the affected director may attend and be counted for quorum if he happens to be a member, his votes as well as those of any members connected to him, cannot count. This rule was not previously the case under common law. 'Interestedness' in the case of 'connected persons' in any case, is an issue for the court to decide.[282]

The requirement for 'disinterestedness,' both in the board and the general meeting, may pose problems in special circumstances, particularly in small, private companies. Where there happens to be a sole director[283] and he is the one involved, the general meeting would have to act, even where the articles say it is the preserve of the board because the latter would have been incapacitated.Where the interests are unified, that is, there is no 'outsider', the question would hardly ever come up for consideration, as there would be nobody to cry foul that there has been a breach of duty. It has been suggested[284] that in exceptional cases whereby all directors' and members' votes are

[281] Note that it is "authorisation" in the case of s. 175, but "ratification" in the case of s.239. In the former occurs before the conduct while the latter takes place after.
[282]Davies, L.P. and Worthington, S. op.cit.at p.602.
[283] Under the new Companies Act, a private company need not have more than one director. See s.154(1) CA.
[284] See Brown, E. (2010). A Case of Split Loyalty?Multiple Directorships and Conflicts of Interests under the Companies Act 2006.*Butterworths Journal of International Banking and Financial Law*, 584 at 585.Retrieved December 24 2013 from www.essexcourt.net/uploads/publications/JIBFL_**brown**.pdf.

excluded, the appropriate course would be for the existing directors to appoint sufficient additional directors that are not in a conflict position.

While some commentators view this new power of boards under s.175 as being proper and consistent with their role as entrepreneurs within the company,[285]--in other words, the right persons to decide these matters—as well as a welcome development,[286] others have expressed worry in the past that this sort of policy has the potential to chip away at the duties directors owe the company and that

> *It is dangerous to allow directors to be judges in their own cause. Surely the board, open to influence from even absent directors, should not delineate the scope of board-members' fiduciary duties. Absolution should come only from a majority of fully informed members...*[287]

This writer quite agrees with the view of Corkery[288] that a watering down of the authorisation regime, as appears to be the case in s. 175, may invite boardroom mischief. This is because management is already powerful as it is and it is the general meeting that is often at a disadvantaged position—chiefly due to having limited information—yet the law is taking away an oversight power that hitherto belonged to the general meeting. It is conceded that the board is ideally the most appropriate organ to decide matters regarding the exploitation of its property, etc. Yet if disclosure is left to the board, it is quite possible that in most cases, the latter would not even report the issue to the general meeting, especially where most members, or an influential member, of the board benefited. In fact, Cokery is of the view that directors, even abstaining or absent, can

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[285]Davies, L.P. and Worthington, S. (2012).Op.cit. at p. 602, footnote 351;

[286] Fitzpatrick, C. (2011). The Companies Act 2006 and its Implications for Company Directors.Being an essay for the 2011 Undergraduate Awards (Ireland) Competition, submitted to the University of Ulster, Ireland.Retrieved December 4, 2013, from http://www.scribd.com/doc/104560914/The-Companies-Act-2006-and-its-implications-for-Company-Directors and GC100. (2008). Companies Act 2006: Directors' Conflicts of Interests. Para 2.7, p. 4. Retrieved December 20, 2013 from www.linklaters.com/pdfs/publications/.../**GC100**briefingpaper.pdf.

[287]Corkery, F.J. op.cit.at p.88.

[288]Ibid. at p.85.

still influence board decisions.[289] However, it is most reassuring that s. 180(1) allows companies which desire to, to reflect in their articles that disclosure be made to the general meeting as well and s.232 voids any provision in the articles which purports to exempt a director of a company from any liability in connection with any breach of duty or breach of trust in relation to the company.

4.2.7 Duty Not to Accept Benefits from Third Parties

Like the section before and after it, s. 176 encapsulates an aspect of the fiduciary rule against making unauthorised gains arising from conflicts of interests while serving the company as part of the general "no-profit" rule recognised by common law. Thus, "A director of a company must not accept a benefit from a third party conferred by reason of—(a) his being a director, or (b) his doing (or not doing) anything as director."[290]

The word "benefit" was deliberately used for the government intends it to admit a wide interpretation, including non-financial gains, gifts and other advantages.[291]Such a third party benefit could be a commission paid to a director personally in the course of his negotiating a business transaction on his company's behalf. Or it could even be profit arising from his taking up in his personal capacity, a business opportunity that had come to him in his capacity as a director of the company, since it came to him "by reason of his being a director." Or it could simply be in the form of free services or waiver of some sort.Thus, free medical service by a doctor for example, or even the waiver of some fee or levy that ought to have been paid by the director, would all fall within the

[289]Ibid. at p.87.
[290]S.176(1).
[291]Per Lord Goldsmith of the Lords Grand Committee at the Committee hearing on 9 February, 2006. See Hansard, Column 330. *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007), p. 12, accessible at http://www.berr.gov.uk/files/file40139.pdf.

prohibition. But in all cases, it must reasonably be regarded as likely to give rise to a conflict of interest.[292]

It has been suggested that moderate corporate entertainment would be unlikely to come under this duty.[293] However, a commentator[294] has expressed worry that a 'too wide' interpretation may blur the dividing line between benefits that are prohibited and corporate hospitality, which is generally considered innocuous. The latter refers to any free entertainment offered by a company to its customers or trading partners, e.g. at major sporting or other public events, as a way of winning over their favour and maintaining good, lasting business relationships.[295] Companies usually have guidelines respecting such corporate hospitality, so that a director would have to ensure that the acceptance of any such hospitality by him from his company's trading partner or client, is appropriate under the circumstances.

The prohibition in s.176(1) also admits bribery. The law has clearly always been against bribery, considering the act of giving and receiving it has been criminalized in every known legal system. The Bribery Act 2010 takes special cognizance of the offence of bribery perpetuated using the corporation. In order to discourage third parties, particularly corporations, from offering bribes, the new Bribery Act criminalizes the failure of a commercial organisation, such as a company, to prevent bribery on its behalf. Such an organisation can be guilty of the offence if the bribery is carried out by an employee, an agent, a subsidiary, or another third-party, as found in s.8 of the law, unless the commercial organisation can show that it had in place "adequate procedures

[292] See s.176(4).
[293] A Guide to a Director's Duties.(2012).Lewis Silkin LLP.pp.5-6. Retrieved January 24, 2014, from http://www.lewissilkin.com/en/Knowledge/2012/January/~/media/Knowledge%20PDFs/Corporate/Guide%20to%20Directors%20Duties.ashx
[294] Chivers, D. (2007). The Companies' Act 2006: Directors' Duties Guidance. The Corporate Responsibility (CORE) Coalition.Retrieved January 22, 2014, from www.thegrid.org.uk/.../hfl/documents/directors_guidance_2006_act.pdf.
[295] Encarta Dictionaries (2009).Microsoft Encarta Premium DVD.

designed to prevent persons associated with [the organisation] from undertaking such conduct."[296] Such procedures may include, not only making provisions in the articles, but also organizing programmes meant to sensitize directors and other employees on the issue and putting in place a system meant to prevent such conducts. For example, as part of their hospitality policy, companiesmay consider maintaining a register of gifts, whichshould be made available for reporting to the board of directors.[297]Setting guidelines and informing its directors, particularly on the issue of corporate hospitality, makes sense because, when a breach occurs, it is usually the company that would sue. Thus, if it does set down guidelines for its directors to follow, they can better guard against breach of this duty, since they would have known the limits their company was prepared to tolerate.

Conducts such as the receiving of commissions or other "benefit," whether financial or otherwise, from *outsiders*, during the course of discharging the duties of the office of company director, receive special attention because the idea is that a director is not allowed to exploit his position in the company for personal benefit, having accepted to serve it in a fiduciary capacity. If the director were to be free to accept benefits from third parties, especially those dealing with his company, there would undoubtedly be a clash of interests[298] in that the director could then be persuaded by the gift/benefit/favour/advantage received from the third parties, to act favourably towards them to the detriment of the company, instead of watching out solely for its best interests or success.

[296] See s.7(2) of the Bribery Act 2010.

[297]Breslin, B., Ezickson, D. and Kocoras, J. (2010). The Bribery Act 2010: Raising the Bar Above the US Foreign Corrupt Practices Act. *The Company Lawyer*, 31(11): 362-369, at 365. Retrieved January 23, 2014 from http://www.mwe.com/info/pubs/Company%20Lawyer%20Issue%2011.pdf.

[298] Or even of *duties*. S.176(5) recognizes that the duty in the section is also infringed if the acceptance of the benefit can reasonably be regarded as likely to result in a conflict of duties.

Since the receipt of such benefits is prohibited, the company is always entitled to sue the director for what he received or its worth, for the director in fact holds it in trust for the company. The Privy Council in **Attorney-General for Hong Kong vs. Reid**[299]established the modern principle that a bribe received by a fiduciary must be held on constructive trust from the moment of its receipt and consequently that any property acquired with that bribe is also held on constructive trust.[300] It also appears that the company can institute an action against such a director whenever it finds out, even if the director has already left its employ. In **Boston Deep Sea Fishing Co. vs. Ansell**,[301] a director of a fishing company contracted for the building of fishing vessels on its behalf. In the course of negotiations, he received a commission from the shipbuilders without disclosing this to the company. Although the company had already dismissed him from office for some other misconduct before it found out about the secret commission, the court held him liable to account to the company for the commission he received.

The rule codified in s.176 potentially covers cases involving any secret profits as well as those involving any secret gain made by a director in the course of a takeover bid, reconstruction or amalgamation involving the company and generally profit derived through the use of confidential information which comes to the director's knowledge through his position on the board.[302] Where the gain happens to be some property or information, s. 175 may also apply simultaneously.[303] In every case, it is no defence for the director to show that he had acted all the while in good faith.[304]

The duty as codified in the Act is as it was under the common law. Perhaps the only changes—or improvement—is the fact that "third party" has been defined and

[299](1994) 1 AC 324.
[300]Hudson, A. op.cit., at p.44.
[301](1888) 39 Ch. D. 339, CA.
[302]Birds, J. et al. op.cit.at p. 652.
[303] S.179 recognizes that more than one of the general duties may apply in any given case.
[304]Birds, J. et al. op.cit.at p. 651.

instances when the duty would not be said to have been infringed, have also been delineated to some extent. Thus, it is now clear that, apart from the company, an associated body corporate or a person acting on behalf of the company or an associated body corporate, every other person is a "third party" within the context of the rule contemplated.[305] From the tenor of the section, instances where the duty would not be said to have been breached are:[306]

1. where the benefits come from the company, an associated body corporate or a person acting on behalf of the company or an associated body corporate;
2. Where a director receives benefits from a person by whom his services (as a director or otherwise) are provided to the company; and
3. Where the acceptance of the benefit cannot reasonably be regarded as likely to give rise to a conflict of interest.

An associated body corporate is the company's holding or subsidiary company or a fellow subsidiary of the same holding company.[307] While the exception in the latter case is quite understandable in the context of group companies, the exception in the case of receiving benefits from a person through whom the director came to his office, whether corporate or natural, is arguable. The director owes his duties to the company, not his nominator. If nominee directors are allowed to get away with corporate benefits in this context, their allegiance would go to their nominators rather than the company, and the nominators could potentially become shadow directors, if their influence on their nominees is considerable.

S.176 makes no provision for board authorisation, unlike s.175 before it. However, the availability of shareholder authorisation at common law is preserved by s.180(4). Further, s.232 also significantly curtails the power of the company to make provisions in the articles exempting or limiting a director's liability for breach of any duty. At least, it would be safe to assume that the company's articles cannot provide that

[305] See s.176(2).
[306] S.176(3) and (4).
[307] See s.256.

directors may legitimately receive third party benefits to an extent in breach of the Bribery Act 2010.

However, s.239 allows the board to ratify what would otherwise have been a director's breach of duty or trust. But it must be noted that the resolution for ratification must be realised without the votes of any affected director, if he were a member.[308] This, the common law permitted, provided at least that the director's breach was in good faith.[309]

It is submitted that the law here seems contradictory. If the general meeting has the power to ratify a director's beach of duty, can't the same general meeting also approve articles which would allow a process for authorising such breach? It is the view of this writer that the general meeting ought not to be allowed to ratify such misconducts perpetuated in the manner described under s. 176. It would amount to fraud on the company.[310]Any commissions/gains/profits/advantages/benefits gained should be disclosed and either declined or accounted to the company, in order to ensure the director's complete good faith in his duties to the company.

It is also curious that the section makes no mention of the "benefit" being "secret" as contemplated by the rule under the common law. Could it be that the benefit is still prohibited even where it is given "openly"? This may be debatable, but it would appear to be the case, at least, for conducts which fit the description of the offence of bribery as provided in the Bribery Act 2010.

This duty also extends beyond the director's tenure so that he would still be bound even after he leaves the company.[311] This effectively discourages the director

[308] See s.239(3) & (4).
[309]Birds, J. et al.op.cit. at p.685.
[310] Granted, the success of the company is "for the benefit of its members as a whole" (s.172), but the company's properties do not in fact belong to the members.
[311] See s. 170(2)(b).

from scheming to resign simply to take advantage of what is being offered, for the company can still go after him to reclaim whatever was given. However, proving that the gift/benefit was in fact given as a consequence of the former director being a director of the company, or doing or not doing something in his capacity as a director at the time, may not be easy for the company.

4.2.8 Duty to Declare Interest in Proposed Transaction or Arrangement

Like the two preceding sections, s.177 covers another aspect of the rule against conflicts of interests. The general rule as set in s.175 is that a director must avoid situations whereby his own interests conflict with those of the company. However, the law seems to make an exception in the case of transactions or arrangements with the company,[312] at least, where the director declares his interests prior to the company entering into the transaction or arrangement with him. In other words, a director is not under a duty to avoid interests in transactions or arrangements with the company. The law simply mandates that "if a director of a company is in any way, *directly* or *indirectly*, interested in a *proposed*transaction or arrangement with the company, he must *declare* the *nature* and *extent* of that interest *to the other directors*."

For some time at common law, it was considered that a director was completely precluded from transacting with the company.[313] Like the general rule against conflicts, any such transactions were forbidden, regardless of the apparent fairness or advantage in favour of the company. Lord Cranworth once justified the rule in the following terms:

> *A corporate body can only act by agents and it is, of course, the duty of those agents so to act as best to promote the interests of the corporation whose affairs they are conducting. Such agents have duties to discharge of a fiduciary nature towards their principal and it is a rule of universal application that no one, having such duties to discharge, shall be*

[312] See s.175(3).

[313] At least, unless any such transaction was also backed by a general meeting approval.

> *allowed to enter into engagements in which he has or can have, a personal interest conflicting, or which possibly may conflict, with the interests of those whom he is bound to protect... So strictly is this principle adhered to that no question is allowed to be raised as to the fairness or unfairness of a contract so entered into...*[314]

This perception may not be unconnected with the notion of the office of the company director being akin to that of a trustee who must never gain from his position. Thus, in **Aberdeen Railway Co. vs. Blaikie Bros,**[315] an early case which considered the issue under discussion, the chairman of the board entered into a contract on behalf of the company to buy a large number of chairs from a firm in which he was 'interested' as a partner. In considering the question whether a director of a railway company is or is not precluded from dealing on behalf of the company with himself, or with a firm in which he is a partner, the Lord Chancellor found it proper to remark thus:

> *His duty to the company imposed on him the obligation of obtaining these chairs at the lowest possible price. His personal interest would lead him in an entirely opposite direction—would induce him to fix the price as high as possible. This is the very evil against which the rule in question is directed...*[316]

However, as observed earlier in this work, it has since been accepted that the similarities between the offices of trustee and company director have limits due to their different job descriptions. The prevalent view is that the director's position is in fact sui generis.[317] Therefore, the restrictions often applicable to the trustee would be particularly unsuitable to the company director. Obviously, outrightly prohibiting the director from transacting with the company may not be good for business in some situations. The director may happen to be the best source of a particular resource

[314] *Aberdeen Railway Co. vs. Blaikie Bros* (1854) 1 Macq. H.L. 461, HL Sc., at 471-472.
[315] (1854) 23 LTR 315.
[316] Per Lord Cranworth LC, ibid. at 316.
[317] Refer generally to **2.6** supra on Status of Directors.

required by the company,[318] and so, prohibiting such transactions may not be in the company's best interests. For example, the director may happen to own property with the best supply of raw materials needed for the company's production. Further, dealing with the director may save the company valuable time, risks and costs.[319] Thus, eventually, the critical issue came to be identifying the proper procedure to be observed in order to rid the director of the taint of conflicted contracting, while allowing him to so contract, rather than observing an outright ban. Thus, in **North-West Trans. Co. vs. Beatty**,[320] a steamer was being built for Beatty, who was both a major shareholder and a director of the North-West Transportation Company. The board resolved to buy the steamer from Beatty. The contract to buy would have been voidable, being in breach of fiduciary duty. However, the resolution to buy had been adopted by a majority of votes at a general meeting, which validated the breach. After first observing that

> *A director of a company is precluded from dealing, on behalf of the company, with himself, and from entering into engagements in which he has a personal interest conflicting, or which possibly may conflict, with the interests of those whom he is bound by fiduciary duty to protect.*[321]

the Privy Council went further to make clear the legal position that Beatty could, as he did, use his votes as shareholder at the general meeting to remedy the defect by ratification. Thus, at common law, the rule came to be that disclosure of the conflict, especially in advance to, and approval of the contract by, the members was the appropriate procedure whereby an interested director could contract with the company.[322] The board's sanction was considered insufficient, even if the 'interested' director did not attend or vote at the board meeting purporting to sanction the breach of

[318]Davies, L.P. and Worthington, S., op.cit. at p.562
[319]Corkery, F.J. op.cit.at p. 81.
[320] (1887) 12 App. Cas. 589.
[321]Per Sir Richard Bagallay, Ibid. at 593.
[322]Davies, L.P. and Worthington, S., op.cit.at p. 562.

duty.[323] Yet, company articles could and often did make provisions allowing directors to engage in self-dealing transactions with little or no restraint and this the courts were more often inclined to uphold.[324]

The duty as codified in the Act restates, and in some instances modifies, the common law in this area. In the first place, s.177 considers indirect interests as well, i.e. where the director himself is not a party, but so closely affiliated to someone who is (whether a company, firm, trust, or an individual), that it can reasonably be assumed that he would also benefit. Thus, it can safely be assumed that, even though the Act does not specifically require disclosure with respect to connected persons, where an immediate family member, or a firm or company in which the director has interests, is interested, then he himself is effectively interested.[325] "Interest" in this context has not been defined by the Act, although it must be one that may "reasonably be regarded as likely to give rise to a conflict of interest,"[326] and not a mere possibility of conflict as earlier contemplated under the common law.[327] However, from case law, it can be gathered[328] that a director can be held to be interested in a contract with another company in which he was a shareholder,[329] or a firm of which he was a member,[330] in a

[323]Corkery, F.J. op.cit.at p.79.

[324]See the cases of *Transvaal Lands Co. vs. New Belgium (Transvaal) Land and Dev. Co*. (1914) 2 Ch. 488; *Peninsular and Oriental Steam Navigation Co. vs. Johnson* (1938) 60 CLR 189 and*Boulting vs. Association of Cinematograph, Television and Allied Technicians*[1963] 1 All ER 716.

[325] Indeed, this was also the case at common law. See*Transvaal Lands Co. vs. New Belgium (Transvaal) Land and Dev. Co*. (1914) 2 Ch. 488; *Newgate Stud Co. vs. Penfold* (2008) 1 B.C.L.C. 46. See further Davies, L.P. and Worthington, S. op.cit. at p.565.

[326] See s.177(6)(a).

[327]See the statements by Lord Cranworth L.C. in *Aberdeen Rly. Co. vs. Blaikie Bros* (1854) 23 LTR 315 at 325 and Sir Richard Bagallay in *North-West Trans Co. vs. Beatty* (1887) 12 App. Cas. 589 at 593 from the earliest cases. But cf. s.175(1). Yet, it was decided in *Boardman vs. Phipps* (1967)2 A.C. 46 that the term 'possibly may conflict' means 'that the reasonable man looking at the relevant facts and circumstances of the particular case would think that there was a *real sensible possibility of conflict*. Indeed, this was the common law position up to the time of the enactment of the present Act.

[328]Birds, J. et al. op.cit.at p. 655.

[329]*Todd vs. Robinson* (1884-1885) 14 QBD 739; *Transvaal Lands Co. vs. New Belgium (Transvaal) Land and Dev. Co*. (1914) 2 Ch. 488).

[330]*Aberdeen Rly.Co. vs. Blaikie Bros* (1854) 23 LTR 315; *Imperial Mercantile Credit Association vs. Coleman* (1873) LR 6 HL 189.

contract to allot shares or debentures to him,[331] and in a debenture granted to release him from a personal guarantee of a debt.[332]

The kind of 'dealing' contemplated by the Act is any "proposed transaction or arrangement." Every kind of contract,from the simplest to the most complex forms, would be covered by this phraseology. There is some evidence that non-contractual arrangements may also be accommodated.[333] However, the use of "proposed" indicates that the transaction or arrangement is merely being contemplated and not yet concluded. The section requires the disclosure to be made before the company fully enters into the transaction or arrangement with the director.[334] Disclosures affecting "existing" transactions are addressed in a different section of the Act.[335]

It is significant that the law requires both the nature and extent of the interest to be disclosed[336] for this would allow for a more informed decision to be made as to whether or not the company should still go ahead with the transaction, in spite of the circumstances. Thus, for example, there is significantly more information in the statement,"A owns 2% of the shares in Z company" than the statement, "A is a shareholder in Z company," or "A is trustee to the beneficial owner of plot XYZ, than simply "A is associated with plot XYZ." Still, there is much sense in Lord Radcliffe's suggestion that "the amount of detail must depend in each case upon the nature of the contract or arrangement proposed and the context in which it arises."[337]

Perhaps, the most significant change introduced by the Act regarding this duty, is in the disclosure regime. As observed earlier, the common law hitherto insisted on

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[331] *Neal vs. Quin* (1916) WN 223; *Cox vs. Dublin City Distillery* (No 2) (1915) 1 Ir R 145.
[332] *Rolled Steel Products Ltd. vs. British Steel Corp*. 1984) BCLC 466 (CA).
[333] See *Re Duckwari (*No.2) (1998) 2 B.C.L.C. 315.
[334] See s.177(4).
[335] Refer to s. 182.
[336] Davis and Worthington consider this "a welcome improvement." See Davies, L.P. and Worthington, S., op.cit. at p.565.
[337] *Gray vs. New Augarita Porcupine Mines Ltd* (1952) 3 DLR 1, at 14.

disclosure to the general meeting as the only organ entitled to allow such conflicts. Thus, disclosure to the board, even a disinterested one at that, was consideredinsufficient. The law then acknowledged the obvious danger that reciprocal self-interest or misplaced loyalty will affect fellow directors' business judgment and affect their zeal to get the best possible deal for the company.[338] Yet, the present Act seems to take a different view as it requires disclosure to be made "to the other directors," rather than the members in a general meeting, effectively making it easier for the 'interested director.' Another obvious conclusion also is that the section does not contemplate such a declaration where there happens to be only one director.[339] Further, the forum and mode of disclosure is also suggested[340] so that the declaration may (but need not) be made— (a) at a meeting of the directors, or (b) by notice to the directors in accordance with— (i) s. 184 (notice in writing), or (ii) s. 185 (general notice). Where disclosure has been made using any of the aforementioned media but subsequently, the director's interest changes or the information earlier given becomes inadequate, inaccurate or incomplete, s.177(3) requires him to make a further disclosure to rectify this.

Helpfully, instances have been delineated where the director would not be duty-bound to disclose any such conflicts arising out of transactions or arrangements with the company. some of these are supported by case law.[341] Accordingly, a director need not disclose such interest[342]

1. where the director is not aware of the interest, transaction or arrangement

[338]Corkery, F.J. at p.79.
[339] However, s.231 requires such a director, where he also happens to be the only member, to record the terms of any such transaction with the company, failure to do which will result in criminal liability.
[340] See s.177(2).
[341] See for example *Cowan de Groot Properties Ltd. vs. Eagle Trust Plc* (1991) BCLC 1045 on reasonable likelihood of conflict, and *Runciman vs. Walter Runciman Plc*. (1992) BCLC 1084 on interest concerning service contract which have been, or are to be, considered by a meeting of directors or by a remuneration committee.
[342] See s.177(5) & (6).

2. if it cannot reasonably be regarded as likely to give rise to a conflict of interest;
3. if, or to the extent that, the other directors are already aware of it; or
4. if, or to the extent that, it concerns terms of his service contract that have been or are to be considered—
   (i) by a meeting of the directors, or
   (ii) by a committee of the directors appointed for the purpose under the company's constitution.

For the purpose of point 1 above, a director is treated as being aware of matters of which he ought reasonably to be aware and this, the drafters consider to be an objective test.[343] It has been suggested that this seems a sensible rider for a director might be excusably unaware of an interest he or she has in a third party contracting with the company or in the transaction.[344] For example, a company in which the director has some shareholding may buy into another company and he may not be immediately aware of this development. A fortiori, the director's son/daughter may have interests in enterprises of which that director may be unaware. Conversely, the law has also effectively excluded ignorance as a defence to a breach of this duty of disclosure. Thus, a director cannot claim to be "unaware" of interests he ought "reasonably" to be aware of.

It is also possible that the other directors may already be aware of the affected director's interests generally, especially in small family companies or where the director's interests are so notorious as to be common knowledge among other board members. A director would therefore not be required to disclose information the other directors know about or ought reasonably to know about.[345] Where the interest concerns

[343]Per Lord Goldsmith of the Lords Grand Committee.*Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 12, quoting from the Committee Report in the Hansard of 9th February 2006, column 334.Retrieved December 23rd 2013, from http://www.berr.gov.uk/files/file40139.pdf.
[344]Davies, L.P. and Worthington, S., op.cit.at p.566.
[345] Refer to s.177(6)(b). See also the cases of *Lee Panavision Ltd. vs. Lee Lighting* (1992) B.C.L.C. 22, particularly at 33; *Runciman vs. Walter RuncimanPlc* (1992) B.C.L.C. 1084; and *MacPherson vs. European Strategic Bureau Ltd.* (1999) 2 B.C.L.C. 203.

his service contract with the company which is, or has been, an agenda item before a directors' meeting or some other such committee, there need not be any formal disclosure by the director.

S.177 simply requires "declaration" and no mention is madeof approval or consent of the company. Thus, whereas 'situational' conflicts (s.175) require prior authorisation to avoid a breach of duty, transactional conflicts (s.177) do not have to be so authorised.[346] The idea is that, when the director declares to the "other directors," who in fact are the proper agents of the company in its transactions or arrangements with third parties, they will then make judicious use of that information. But that is not to say that the company may not take any action further than that. S.180(1) hints that the company may enact provisions in its articles having additional requirements, for example, that the members give their approval or consent to the company entering into such dealings with the director. This would be desirable particularly for public companies.

Further, there is a potential problem, as with s.175 discussed above, in a situation where most of, or all, the directors happen to be 'interested'. Here, the law wouldobviously be handicapped, unless the members come in. This is more so as s.177 does not even require disclosure to a 'disinterested' board.[347]Two uneasy conclusions can be drawn from this. One is that s.177 does not contemplate disclosure in the case of a company with a sole director.[348] The other is that an interested director, barring any provisions in the company's articles stating otherwise, can participate in decisions concerning his own transactions with the company. It is curious that s.177 does not address this. Does this mean that simply declaring to the rest of the directors, even if

[346]Source: http://www.manches.com/Content/Resources/files/publications/directors-duties-conflicts-of-interest-2013.pdf accessed 5th February, 2014.

[347] Again, recall that s.175(3) specifically ousts conflict situations arising from transactions with the company from applying under that section.

[348] According to s.154, a private company can have just one director.

they happen to be cronies of, or connected to, the affected director, suffices? If this is the case, then the conflicting director, if he has enough influence on the board, could quite easily get away with things.

Others[349] are also of the view that disclosure ought to be to the general meeting. According to Gower, "it hardly seems over-cynical to suggest that disclosure to one's cronies is a less effective restraint on self-seeking than disclosure to those for whom one is a fiduciary."[350] Indeed, it would be dangerous to allow directors to be judges in their own cause.[351] There certainly is logic in the suggestion that the procedure in all cases of conflict of duty and interests, i.e. from ss.175-177, should be the same.[352] It is submitted that arguments in favour of disclosure to and approval of the general meeting advanced in the discussion regarding s.175 supra, also apply here. Or at least, the rule be enforced that the matter, even after disclosure, should be considered by a disinterested board and in the absence of such a board, by the general meeting.

As for existing—as opposed to "proposed"— transactions or arrangement, s.182 requires a director of a company who is in any way, directly or indirectly, interested in a transaction or arrangement that has been entered into by that company, to declare the nature and extent of the interest to the other directors in much the same manner discussed above under s.177, unless already made. Only the three aforementioned modes of disclosure are allowed. Such a declaration is required to be made "as soon as is reasonably practicable."[353] But the declaration is not required where the director is not aware of the interest or of the particular transaction or arrangement in question,

[349]Such as Davies, L.P. and Worthington, S.op.cit.andCorkery, F.J. op.cit.
[350] Gower, L.C.B. (1971). Principles of Modern Company Law. 4th ed at 587.
[351]Corkery, F.J. op.cit.at p.88.
[352] Worthington, S. Op.cit. at pp.12-13.
[353] See s.182(4).

though he is treated as being aware of matters of which he ought reasonably to be aware.[354]

Importantly, unlike failure to declare under s.177 which results in civil consequences,[355] failure to so declare under s.182 will attract criminal liability.[356] It is not immediately clear why this is the case. Perhaps, the presumption is that there would be less civil remedies available to the company, such as rescission or avoidance, in the case of existing transactions. Furthermore, where the director's interests is so intertwined with a third party's, it may not be easy to ascertain the exact amount of benefit he gained, so as to resort to disgorgement, i.e. force him to account for the profits.

Where there is a sole director in a public company, the sole director must record the nature and extent of his interest in any transaction or arrangement in writing and this is deemed to form part of the proceedings of the next meeting of the directors and must be properly minuted.[357] Also, where any sole director happens to contract with the company while being its only member, he is required to set down the terms of any such contract in writing or record them in the minutes of directors' meeting.[358]

With respect to a shadow director, the applicability of the duty is not clear. This is because, although s.170(5) clarifies that all the general duties apply to shadow directors where, and to the extent that, the corresponding common law rules or equitable principles so apply, it is not in fact clear whether the duty of disclosure was applicable to shadow directors under common law.[359] In fact, the whole idea about the shadow

[354] See s.182(5).
[355] See s.178(1).
[356] Refer to s. 183. It is curious that the Act does not also grant the company the right to avoid or rescind the contract as well, as is the case with proposed transactions.
[357] See s.186.
[358] See s.231.
[359] Davies, L.P. and Worthington, S., op.cit.at p.564.

director owing fiduciary duties is debatable.[360] In **Ultraframe UK Ltd vs. Fielding**[361] the High Court stated that "*the indirect influence exerted by a paradigm shadow director who does not directly deal with or claim the right to deal directly with the company's assets will not usually...be enough to impose fiduciary duties upon him.*" At the most, it appears that he would owe the duty to act in good faith towards the company only in relation to the directions or instructions he gives the others.[362] Davies and Worthington are also aligned to this view,[363] although generally, case context is all-important.[364]

Curiously, the shadow director is expressly obligated to disclose existing transactions or arrangements with the company.[365] Why the same is not the case for proposed transactions, is unclear. It has been opined,[366] and this writer subscribes to the opinion, that it is more imperative for the shadow director to disclose proposed than existing transactions, considering the company may not have the opportunity of pulling out in the case of the latter, unlike the former.

S.182 imposes upon a director a new and continuing duty to disclose, where he fails to disclose the interest in the beginning. Thus, if for whatever reason the director fails to disclose in the beginning (at the contract stage), he is still obliged to disclose even after the company commits itself to the transaction or arrangement, in spite of the fact that the company may not have the opportunity to rescind. Connected as s.177 is to s.182, it is curious that the sections are so far apart or not incorporated.

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[360] See Birds, J. et al. op.cit. at p.580 footnote 27 and pp.626-627.
[361] (2005) EWHC 1638 Ch.
[362] See ***Vivendi SA vs. Richards* (2013) EWHC 3006.**
[363] See Davies, L.P. and Worthington, S., op.cit. at p.514.
[364] Mackenzie, G. (2013). *Shadow Directors and their Duties*. Walker Morris LLP. Retrieved 2nd March 2013 from http://www.walkermorris.co.uk/shadow-directors-and-their-duties.
[365] See s.187.
[366] Davies, L.P. and Worthington, S., op.cit. at p. 564

CHAPTER FIVE

COMPARATIVE EVALUATION

5.1 Introduction

This work acknowledges the similarities and common origins of the two legislations on the topic under review. This is particularly referring to their equitable and common law foundations. However, each law was enacted in a different period: the Companies and Allied Matters Act 1990,[1] "CAMA" in the early '90s and the Companies Act "CA" rather early in the 21st century. It can therefore be safely assumed that the latter law would be more current and up to date with developments in case-law and business practice. In spite of this, the very basic principles of law on directors' duties developed since the early beginnings of the concept of the company, remain in place.[2]

A cursory examination of the statement of duties under the CAMA suggests it is ambiguous in many respects. The direction of the CA is commendable and makes much sense in many areas. In some aspects, however, the latter law is controversial and therefore not recommendable.

5.2 General Observation

From a general examination of the CA, the later of the two laws, the law appears to embrace the principle of a freer economy, whereby the state seeks to, as much as possible, deregulate the running of enterprises by simply laying ground rules for basic regulation and leaving the rest to investors.[3] This is informed by the fact that the CA allows for one-man companies[4] and boards.[5] A company may also do without a

[1] Cap C20, Laws of the Federation of Nigeria 2004.
[2] For example, the principle that the duties of directors are owed to the company alone and that only the company can enforce the directors' duties and also that the director's business decision is evaluated by subjective standards.
[3] Davies, L.P. and Worthington, S. (2012).*Gower & Davies: Principles of Modern Company Law,* 9th edition, Sweet and Maxwell, London, p. 64.
[4] See s.7(1) CA.
[5] See s.154 CA.

company secretary.[6] The CA also abolishes the requirement for companies to state their objects in the memorandum. Therefore, unless a company's articles specifically restrict its scope, its objects are unrestricted.[7] Thus, members could easily decide at every turn, what the company should aim to achieve. Furthermore, situations of conflicts of interests are more often left to the decision of the company through the articles.[8] In fact, a 'disinterested' general meeting is allowed to ratify any conduct by a director amounting to negligence, default, breach of duty or breach of trust in relation to the company.[9] It is thus apparent from the codified duties of directors that the rules have changed and have been 'loosened' in order to allow companies to be run in the way the members, who are in fact the residual owners, determine that they should be run, with minimum interference from the state.

Thus, it would appear the modern approach towards encouraging enterprises is deregulation, as opposed to the approach apparent in the CAMA, which is characterized by considerable state regulation in the running of companies in a bid to stifle fraud and as much as possible, prevent mismanagement. This tone is evident in the tenor of the law.[10] Thus, a minimum of two persons is required for incorporation;[11] even small limited companies still require a minimum of 2 directors[12] in addition to a company secretary;[13] and companies objects are restricted to those mentioned in the memorandum,[14] alteration of which requires considerable technical procedures.[15] Many of the rules relating to directors duties under the CAMA cannot be altered by the

[6] See s.270 CA.
[7] See s.31 CA.
[8] S.180(4)(b) CA allows the articles to make provisions dealing with conflicts of interest.
[9] See s.239 CA.
[10] The CAMA is more often in mandatory terms so that companies have no discretion to exercise in certain matters.
[11] See s.18 CAMA
[12] See s.246 CAMA.
[13] See s.293(1) CAMA.
[14] See s.39(1).
[15] See ss.44, 45(2) and 46 CAMA.

articles.[16] Arguably, it may be that the sum total of these principles is the discouragement of incorporation, especially by sole proprietors or one-man business owners who would not want to share control, no matter how insignificantly. Therefore, the approach of each of the two legislations in relation to directors' duties, is reflective of other aspects of company law within the respective legislations.

In terms of structure and general style, the CA has much to commend it over the CAMA. First, the sections regarding the general duties of directors are arranged sequentially, so that they are found in the same part of the Act. Thus, the duties run from ss.171 to 177. The only other related aspect separated, owing to having a different consequence of breach, is the duty of disclosure with respect to existing transactions. Second, the language used in the sections aimed at achieving simplicity, clarity and unambiguity.[17] In fact, this is the most obvious aspect of the codification of directors' duties in the CA. The achievement of this feat was aided in part by the use of introductory sections and subsections that helped to further clarify the main substantive provisions. This is the case with ss.170, 174(2), 175(2), and 176(2). Also, exceptions to the rules in each section regarding each duty, have been clearly stated. Third, the provisions are made in a language general enough to admit judicial activism in order to further develop the law in practice. This is especially evident from the admission of 'reasonability' in determining breach in some cases. Finally, the duties are couched in more proper language that effectively reduces the principles developed under common law, into the proper tone of obligation. Thus, all the sections begin thus, "A director of a company must…"

[16] See s.279(8).

[17] Part of the terms of reference for the CLRSG was modernising company law in order to provide a simple, efficient and cost-effective framework, drafted in clear, concise and unambiguous language which can be readily understood by those involved in business enterprise. See Appendix A to the CLRSG Final Report, July 2001. Retrieved October 4, 2013, from http://www.dti.gov.uk/cld/review.htm.

These commendable characteristics are not observable in the CAMA. Here, the sections on the topic are not sequentially arranged, with aspects of allied principles dispersed within the provisions. For example, conflict of interest principles in s.280 are separated from allied principles on self-dealing and secret benefits in ss.277 and 287. The same is true of the duty to act in good faith, which is to be found variously in ss.279(1), (3) and s.282 as well as the duty to exercise care and skill captured in ss.279(3) and 282. The language of the law in the CAMA in some cases, is either ambiguous and therefore, unclear, or even downright misleading. This is observable in ss.279(1), (2), (3), (4), (5) and (6). Furthermore, although also constituting "duties of directors", the principles captured under ss.280, 282 and 287 have, apparently inadvertently, been excluded from the ambit of the rule in s.279(9), which requires the company to enforce the duties of directors.Thus, the arrangement of the relevant sections on directors' duties in the CAMA disrupt a good flow of the law: the CA is better on this point. In fact, the statement of duties under the CA would be more comprehendible to a director of average acumen than the provisions of the CAMA. In the latter case, the director may have to go through a horde of court decisions or pay substantial professional fees in order to find out their proper interpretation.

Both legislations in principle require the duties to be observed by every director, presumably both de facto and de jure. However, their applicability to shadow directors is not clear. The CAMA specifically imposes the obligations in s.281 on the shadow director as a multiple director.[18] The said section requires him to observe the fiduciary duties, particularly those against conflicts of interests and duties. On the other hand, the CA simply states that the general duties are applicable to shadow directors to the extent applicable to them under corresponding common law and equitable principles, while it

[18] See s.245(1) CAMA.

is not clear the extent to which they were so obliged under those two. However, more recent judicial decision in the UK suggests that the shadow director owes the duty to act in good faith towards the company at least in relation to the directions or instructions he gives the others.[19] Apparently, case context is all-important.[20] But it has been argued,[21] and this writer subscribes to the opinion, that the general duties should apply to shadow directors, at least to the extent that the shadow directors have exercised control over the board.

It is noteworthy that the duties codified under the CA are complemented by other legislations such as the Company Directors Disqualification Act 1986, and the Insolvency Act 2000. There appears to be no legislation supportive of the CAMA on directors' duties.[22]

5.3 Comparative Analyses

In the last two preceding chapters, this work considered the statutory provisions on directors' duties available in both legislations, where some ambiguities were observed in the CAMA and also criticisms noted regarding some aspects of the duties codified under the CA. Presently, this work compares the two laws on the issue under consideration, seriatim.

The duties codified under the CAMA have been referred to as "the principles on which the duties of directors are based."[23] This is due to the fact that, although the CAMA heads s.279 "duties of directors", much of the content of the section is merely making statements of principles of law, rather than requiring the director to do a

[19] See ***Vivendi SA vs. Richards*(2013) EWHC 3006.**
[20] Mackenzie, G. (2013). *Shadow Directors and their Duties*. Walker Morris LLP. Retrieved March 2, 2013, from http://www.walkermorris.co.uk/shadow-directors-and-their-duties.
[21] Davies, L.P. and Worthington, S., op.cit.at p.514.
[22] Though there are a number of related provisions in legislations which are industry-specific and therefore not applicable to directors generally. For example, BOFIA.
[23] See Orojo, J.O. (2008).*Company Law and Practice in Nigeria*.Durban, South Africa.5th edition. LexisNexis Butterworths, p.266.

positive act, which a 'duty' normally entails. The same can be said of other sections on the topic. On the other hand, as earlier observed, the drafters of the CA have cleverly—and, this writer submits, more appropriately—transformed the various legal principles on directors duties developed over time, into positive duties. Thus, each of the seven duties discussed under Chapter Four of this work begins thus, "a director of a company must…" To make the work under this chapter easier, therefore, the duties will be compared under the headings, and in the order in which they appear, in the CA.

5.3.1 Duty to Act Within Powers

The duty here is codified under s.171 of the CA and states that "a director of a company must (a) act in accordance with the company's constitution, and (b) only exercise powers for the purposes for which they are conferred". The duty is captioned "to act within powers" and the provisions thereunder clearly amplify what that statement requires. The important pointer here is the reference to "the company's constitution" as the source of that power within which the director is required to act.

Early in the CA, s.17 clearly explains what "the company's constitution" entails as including the company's articles and any resolutions or agreements applicable under s.29 of the CA. As pointed out earlier in this work,[24] this effectively grants the general meeting reserve powers to order the board to do or refrain from doing an act, simply by passing a special resolution. In other words, the general meeting would not constantly have to resort to the lengthy process of altering the articles in order to request the board to act in a certain way, particularly where time is of the essence.

Under the CAMA, the equivalent of the duty under review is codified under s.279(5) as discussed earlier in this work.[25] It has been observed that the language of the law confuses, rather than clarifies what exactly is required of the director. The law says

[24] Refer back to **2.7** on Division of Power between the Directors and the General Meeting and **4.2.2** on Duty to Act Within Powers, supra.
[25] Refer to **3.5** supra on "Duty to Act in the Best Interests of the Company and for Proper Purpose."

"a director shall exercise his powers for the purpose for which *he* is specified and shall not do so for a collateral purpose, and the power, if exercised for the right purposes does not constitute a breach of duty, if it incidentally affects a member adversely." There are about four discernible issues with this provision, as earlier discussed.

First, if a director has any powers by himself, it is not clear from the provision what they are or where he is likely to find them. Generally, whatever powers directors wield are not in fact theirs but the company's. Also, when they act, they act as a collegiate body, although they owe their duties individually.[26] Yet, here the law speaks of "his powers". Second, the part stating "he is specified" does not make much sense because the provision is obviously alluding to "the powers" mentioned earlier. Thus, the pronoun "he" ought to read "they" in order to properly refer to the powers, which are the proper subjects being addressed. This assumption is further supported by the later statement, "and *the* power…." Third, the subsection initially mentions "his powers" i.e. in the plural, but later refers to "the power", in the singular, and further confounds this with "purposes," also in the plural. Fourth, the use of the qualifier "specified" suggests that the powers are contained somewhere. But the provision neglected to at least refer to the likely source.

The cumulative effect of these observations is to render the provision unclear. It is hardly the intention of the drafters that this should be the case. It is submitted that, for a director to properly discharge his duties here, the law ought to be clear regarding a critical issue such as "his powers." It is important that the law here should not be so ambiguous as to be beyond the comprehension of a director of average acumen.

One would need to comb through other parts of the CAMA in order to learn of the likely powers and power sources of the director. The combined effect of s.63(1) and

[26] See s.282(3) CAMA.

(2) is to allow the articles to specify the powers of the directors as a board, acting for the company. It can safely be assumed that whatever individual powers the directors have would also be stated in the articles. By s. 63(3), it is clear that the board also exercises the residual powers of the company. The general meeting may come in only in the four instances listed under s. 63(5). Thus, if the general meeting requires the directors to act in a certain way or refrain from doing anything within their powers under the articles, the general meeting would need to go through the cumbersome process of altering the articles to reflect that. It is submitted that this fact and the automatic allocation of residual powers to directors, further subordinates the general meeting to the management.

Evidently, s.171 of the CA is comparatively the better provision over s.279(5) of the CAMA for obvious reasons. First, the former provision is straightforward and hardly needs any further clarification. Second, the CA rightly recognizes that the powers to be exercised by the director are those of the company. Importantly, the source of the powers has been identified as the company's constitution, while the constituents of the constitution have been properly stated. A significant aspect of these constituents is the resolution of the general meeting. It is submitted that this power of the general meeting better provides the much needed check to the powers of the directors.

Thus, although upon proper interpretation, both provisions are interpreted substantially the same way in practice—having both recognized the articles as the primary source of the directors' powers—still, s.279(5) would have to be redrafted if the law therein is to make proper sense. Adopting the tenor of s.171 of the CA will not do without first recognizing the resolution of members as a potential source of power of the directors. However, even without this, the law can still be redrafted to accommodate the articles.

5.3.2 Duty to Promote the Success of the Company

This duty is perhaps the most controversial of the duties of directors codified in the CA.[27] From parliamentary debate to enactment, it raised several questions, including the meaning of success, the extent to which the interests of other groups outside of members, can be favoured, and importantly, the matter of its enforceability. In the end, theCompany Law Review Steering Group (CLRSG), which was saddled with the responsibility of making proposals for the new legislation, went ahead to introduce the novel concept of enlightened shareholder value (ESV), which is neither based on shareholder primacy nor the stakeholder principles,[28] but adopts aspects of both. S. 172 provides, inter alia, that

> *(2)A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—*
> *(g) the likely consequences of any decision in the long term,*
> *(h) the interests of the company's employees,*
> *(i) the need to foster the company's business relationships with suppliers, customers and others,*
> *(j) the impact of the company's operations on the community and the environment,*
> *(k)the desirability of the company maintaining a reputation for high standards of business conduct, and*
> (l) *the need to act fairly as between members of the company.*

The premise upon which the CLRSG proposed a section like 172 was that"the state of directors' duties at common law are often regarded as leading to directors having an undue focus on the short-term and the narrow interests of members at the expense of

[27] Refer to **4.2.3** supra for more discussions on this point.
[28] For detailed discussion on these, refer to **3.4.2** supra on In Whose Interests and for Whose Benefit Should Directors Manage the Company.

what is in a broader and a longer-term sense, the best interests of the enterprise."[29] Thus, the section is intended to address the issue of short-termism, which is reputed to be the major cause of corporate failure in recent times.[30]

The section contains the foremost fiduciary duty of directors. They are required to act always in good faith with the aim of promoting the success of the company. The idea of *success* is left to be defined by every company to suit its objective. But importantly, it is to be achieved ultimately for the benefit of the members as a whole, and if the company is not pro-profit, achieving whatever purpose for which the company was set up. The section then lists a number of factors which every director must consider in arriving at his decisions, including the company's employees, host community, the environment and the need to act fairly as between members. This is in addition to any others the director might wish to consider. The provision is further supported by a requirement for business review under s.417 of the CA, in which the directors would state how, if at all, they have performed their duty under s.172, to be presented before the general meeting as part of the (annual) directors' report.

Much as the section set out to satisfy all (varied) interests, there have been more criticisms than commendations regarding it. This work has already considered these in great detail in the previous chapter.[31] However, a recap of the main points is apposite, here.

First, the law allows a director to act in a way "he considers…most likely to promote the success of the company", but goes further to suggest to the director some factors for his consideration. In other words, the law acknowledges the legitimacy of the director's subjective business judgement, yet, as Hollington puts it, proposes to teach

[29] Company Law Review *Modern Company Law for a Competitive Economy*: The Strategic Framework (London, DTI, 1999) at para 5.1.17.
[30] Refer back to **4.2.3** supra for more discussions on this.
[31] Further refer to **4.2.3** supra.

businessmen how they should make business decisions.[32] Second, the factors and interests listed are varied and the government has clarified that none of the items is superior to the others. Where a director is faced with two or more competing interests—as will more often be the case—how does he prioritize? Even stakeholder theorists admit the enormity of such decisions.[33]

Lastly and more importantly, how is the law to be enforced? In other words, since the government has clarified that "have regard to" means simply to "think about,"[34] where a director takes a decision without actually "thinking about" these factors, how can a breach of the duty be proved and who is to hold him responsible? The requirement for a business review does not adequately address this problem because, in the first place, not all companies are required to prepare one. Besides, it is meant to be part of the directors' report, the primary recipient of which is the "the company" in a general meeting. Thus, the various stakeholders, whose interests are meant to be *regarded*, do not have access to that report as of right. It goes without saying that, unless the company has incidentally incurred losses by a director's decision, "it" will not indict him for breach of duty on behalf of, say, the environment or customers whose interests have been *disregarded*in arriving at a particular decision.

Few courts have so far had the chance to interpret s.172 in their deliberations. However, already, some[35] speculate that not much has been changed from the closest

[32]Hollington R. (2008).*Directors' Duties under the Companies Act 2006: Have the Lunatics Taken Over the Asylum?* A lecture delivered at Ian Fairbairn Lecture Theatre, University of Buckingham, (April 22, 2008), pp. 4 and 7. Retrieved March 23 2013 from http://www.newsquarechambers.co.uk/files/Publications/Directors%20duties%20under%20the%20Companies%20Act%202006%20(Robin%20Hollington%20QC).pdf

[33]Freeman, R.E. *et al.* (2010). *Stakeholder Theory: The State of the Art*. New York.Cambridge University Press, p. 28.

[34]*Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 11, Hodge MP in the Commons Report of October 17 2006, Column 789 of the Hansard, accessible at http://www.berr.gov.uk/files/file40139.pdf.

[35] Including Lord Glennie in *Re West Coast Capital (LIOS) Ltd*. (2008) CSOH, 72; 2008 Scot (D) 16/5 (Outer House, Court of Sessions, Lord Glennie at 21; Warren J. in *Cobden Investments Ltd. vs. RWM Rangport Ltd*. (2008) EWHC 2810, (Ch); Birds, J. et al. (2011).*Boyle and Birds' Company Law.*8th edition, Jordan

common law antecedent of the duty and that whatever development made thereto is, at best, modest. In fact, nothing previously prevented directors from considering any of the listed factors under the law.[36] Proponents of both stakeholder and shareholder primacy business theories have found fault with the provision.[37] The main point in these criticisms is that nothing is likely to change in the attitude of directors in their decision-making. In fact, an empirical study undertaken by Taylor[38] indicates that the pressure on short-termism in favour of more long-term thinking had not been reduced since the enactment of s.172.

In the case of the CAMA, the near-equivalent of the duty just discussed is captured under s.279(3) and (4), as discussed earlier.[39] The law therein provides that

> *A director shall act at all times in what he believes to be the best interests of the company as a whole so as to preserve its assets, further its business, and promote the purposes for which it was formed, and in such manner as a faithful, diligent, careful and ordinarily skilful director would act in the circumstances.*
> *The matters to which the director of a company is to have regard in the performance of his functions include the interests of the company's employees in general as well as the interests of its members.*

Here, the corporate objectives of the powers wielded by the director under the CAMA, are stated. Like s.172 of the CA, in s.279(3) CAMA, the director's subjective judgment is clearly sanctioned: it is open to scrutiny only by his standards and none other's, for as long as he acts for the proper purposes. Further, s.172 CA requires the consideration of

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Publishing Limited, Bristol, pp. 637-638; Davies, L.P. and Worthington, S. (2012).Op.cit. at p. 543; Tate, C.R. (2011).*S. 172 CA 2006: The Ticket to Stakeholder Value or Simply Tokenism?* Being term paper submitted to the Graduate School of Law, University of Aberdeen, pp. 2, 3 and 8; Keay, A. (2007). Tackling the Issue of the Corporate Objective: An Analysis of the United Kingdom's Enlightened Shareholder Value Approach.*Sydney Law Review.* 29: 577-612, at 604, 610 and 611.

[36] Though s.309 of the Companies Act of 1985 only mentioned the interests of employees and members in general, the section could be interpreted to accommodate other corporate stakeholders.

[37] Refer extensively to **4.2.3** supra.

[38] Taylor, P. (2010). *Enlightened Shareholder Value and the Companies Act 2006.*(Unpublished doctoral dissertation).Birbeck College, University of London, England, p. 162. Retrieved May 24, 2014, from http://www.lccge.bbk.ac.uk/publications-and-resources/docs/PhDThesisPNTaylorJune2010.pdf.

[39] Refer extensively to **3.4** supra.

the matters mentioned and admits those not necessarily mentioned in the list of factors provided, just as s.279(4) CAMA also does the same. But the similarities end here. The differences are more significant. First, where s.172 of the CA refers to "the benefit of its members as a whole," s.279(3) of CAMA on the other hand refers to "the best interests of the company as a whole." Second, where s.172 CA refers to the "success of the company," s.279(3) CAMA mentions the best interests of the company…so as to preserve its assets, further its business, and promote the purposes for which it was formed." Third, where s.172(1) lists six matters to which a director must have regard among others and report this per s.417 CA, s.279(4) CAMA simply mentions the employees in general and members. This is in addition to the fact that s.172(3) CA admits the modification of the main duty under s.172(1) CA under circumstances in which the interests of creditors of the company would have to come first. Finally, where s.172 CA requires the director to act "in good faith" s.279(3) CAMA demands of him to act in the manner of a faithful, diligent, careful and ordinarily skilful director."

There is need to consider these differences in more detail. Earlier in this work, the issue of the separate identity of the company was mentioned.[40] Both laws are clear that the duties of directors are only owed the company.[41] And the question of any duty to individual shareholders does not arise under statutory law.This follows from the issue of enforceability: only the company can enforce the duties its directors owe it.[42]The fact is, no one owns the company: at best, a shareholder only has a transferable interest. However, the courts have consistently aligned the "interests of the company" with the "interests of members," since the company is a mere legal fiction that exists only in the

[40] Refer to **3.4.2** supra on In whose Interests and for whose Benefit should Directors Manage the Company?
[41] See s.279(9) CAMA and s.170(1) CA, discussed under **3.4.2**and **4.2.1** supra.
[42] Refer to s. 279(9) CAMA and s.178 CA.

eyes of the law, having no eyes or brains of its own.[43]Thus, "interests of members" was believed to be akin to the interests of both present and future members,[44] since it was understood as technically impossible to assign any interests to the artificial entity called "the company" by itself, without relating it to the interests of human persons.[45] Yet,by mentioning "interests of the company" and "interests of the members" in different subsections, the CAMA implies that these are not in the same category.

Besides, who is *the company?* If the directors were to abandon the interests of the company in favour of the interests of the shareholders—say, by declaring a dividend instead of recapitalizing to expand operations or employing better skilled labour—who would bring the directors to book in such a situation? Obviously, not the shareholders in whose ultimate favour the directors might have acted, and surely not the directors themselves. Unfortunately, these are the only "organs" through which the company might have acted in order to redress the "wrong". Under the circumstances, therefore, it is hardly surprising that to date, there has been no report of an action to enforce the employees' aspect of s. 279(4) CAMA. The same is true of s.172 CA.

Thus, it was argued earlier in this work,[46]that owing a duty to the company is *in fact* owing a duty to "its members" collectively, for, although the company is established as having a separate and distinct personality from those of its members,[47] it is in fact for the ultimate benefit of the members collectively, whose "association" initially formed the company,[48] that the company exists. At least, this is true of the more prevalent limited liability company. More importantly, the members can enforce the directors'

[43]*Ladejobi vs. Odutola Holdings Ltd.* (2002) 3 NWLR (Pt.753) 121 C.A.
[44]*Brady vs. Brady* (1987) 3 BCC, 535 at 552 (CA); *Gaiman vs. National Association for Mental Health* (1971) Ch. at 330.
[45] Even where a company is wholly made up of artificial persons, some natural persons somewhere down the line will be receiving the profits.
[46] Refer to **3.4.1** supra on Owed to Whom?
[47]*Salomon vs. Salomon & Co. Ltd.* (1897) A.C. 22.
[48] Refer to s.37 CAMA and s.7(1) CA.

duties through their powers in the general meeting,[49] or derivative actions. For these reasons, law more appropriately reflects fact when it requires the director to act for the benefit of members as a whole, than when it requires that he act in the best interests of the company as a whole. A fortiori, directors may owe their duties to the company in *law*, but they owe them to the collectivity of the members of the company in *fact*. Thus, one commendable aspect of s.172 is in its recognizing this fact. Clearly, s.279 of the CAMA does not reflect this reality. Even though s.283 of the law mentions that directors shall exercise their power "in the interest of the company and all the shareholders," this statement is far removed from the statement of the fiduciary duties four sections away, and appears to be directed at cautioning directors against furthering their self-interests.

But, whatdoes s.172 mean by success in relation to the company? Parliament has indicated that it has deliberately left this question to each company to answer for itself.[50] However, for a limited liability company, it can safely be assumed that the notion of success would involve a balance sheet heavier on the credit side and more returns for its shareholders. But it is also possible that for some companies, success is translated in terms of ousting competitors, opening new frontiers, achieving more fame or even "greening" their operations. This is also bearing in mind that companies are set up for every kind of known lawful business. For charitable or other such companies with altruistic motives, it is conceded that success would take an entirely different dimension.

Evidently, *success* is a very nebulous term which, in the area of companies, cannot easily be pegged down to a specific definition. Thus, when s.279(3) CAMA speaks of preserving the company's assets, furthering its business, and promoting the

[49] These powers include removal of directors and appointment of new ones and holding resolutions towards instituting an action in the name of the company.

[50] Per Lord Goldsmith of the Lord's Grand Committee of Parliament. See *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 9, quoting the Hansard of February 6, 2006, column 255, accessible at http://www.berr.gov.uk/files/file40139.pdf.

purposes for which it was formed, it is clear that, the law in attempting at the idea of the "best interests of the company" has clearly presented a restricted objective for the establishment of companies. A company may not want to hold on to its assets and may in fact desire to liquidate them all, at a particular point in time. A company may also be set up simply for a specific purpose to be achieved within a limited time, so that "furthering its business" may not really be in its best interests. It may even want to sell off or merge with another. The purposes for which a company is formed may change over time, as it is clearly lawful for it to go into any kind of lawful business. Conclusively, therefore, the idea of the company's objective or success is better left to it to decide, for this is obviously not the province of corporate law. It is submitted that s.172 CA is more realistic than s.279(3) CAMA for recognizing that the company's success is for the benefit of its members and is ultimately for it to decide. This duty can always be modified by a proviso, in the case of charitable companies or companies limited by guarantee, to be towards achieving whatever purposes for which they were set.[51]

As for matters to which directors are required to have regard under the two laws, stakeholder theorists have for some time advocated the idea that the corporation as an entity, acting through its directors, owes a duty to consider the interests of all its stakeholders equally, without giving one constituency primacy over the other. Thus, interests of other groups affecting or being affected by the company should be considered in the same manner as the interests of shareholders. But the tone of both laws under review negates this philosophy in favour of shareholder primacy.

In the case of s.172 CA, clearly, "the benefit of members as a whole" comes before the interests of all the factors in the list thereunder. In fact, the listed factors are to

[51]Interestingly, though, the idea of the objectives of the company under s.279(3) CAMA can accommodate all kinds of companies, whereas that under s.172(1) had to be modified by subsection (2) for charitable companies. But these companies are far less prevalent.

be considered only to the extent that their interests promote the success of the company f*or the benefit of its members*, so that, where the interests of the factors would be to the detriment of that objective, they would be jettisoned. The CLRSG, by introducing the concept of ESV, intend for the rules to be different, because of the list of factors to which it is mandatory to have regard. But in fact, the introductory statement in s.172 CA clearly reaffirms the shareholder primacy norm long established within the jurisdiction. In the absence of voting power/ownership rights co-equal with those of members, the interests of the other factors under the section will not improve much.

It is important to understand that s.309 of the Companies Act 1985 was exactly like s.279(4) CAMA. The provision has previously been dubbed some disturbingly unpleasant names, including "a mere pious declaration"[52] and "a lame duck provision,"[53] particularly owing to the fact that hardly any cases have been reported regarding its breach because of the obvious difficulty employees would have encountered regarding proof.[54] Thus, s.172(1)(a)-(f) CA is intended to improve on it. S.279(4) CAMA can admit all the factors listed under s.172 and more, although the director is required to actually consider the members and employees. Recall that some of the criticisms regarding s.172 CA essentially point out that it is not for the law to tell the director, who has the job description of a business man, how he should arrive at his business decisions. In other words, since the law grants him the leverage to act "in the way he considers"—or as the CAMA states, "in what he believes"—it is therefore not for the law to encroach into the director's subjective judgment by further suggesting to him the interests to which his actions must tend to promote, particularly when the law has already begun by

[52]Ogbuanya, N.C.S. (2010).*Essentials of Corporate Law Practice in Nigeria.*Novena Publishers Ltd., Lagos, p. 337.
[53]Keay, A. (2007).Op.cit.,at p. 593.
[54] Ibid.

stating the prevailing interest he is serving (the benefit of members as a whole, in the case of the CA, and the benefit of the company as a whole, in the case of the CAMA).

Recall that it was noted supra in this work how placing the interests of members, on the one hand, and those of others, such as employees, as the more prominent stakeholders of the company, is inappropriate, considering the fact that the two groups do not have the same powers to wield over directors, nor do they have comparable interests. The interests of the members would most likely be akin to the interests of the company, especially since the members can decide the company's objectives at any given time. On the other hand, the interests of employees would most certainly be towards securing their jobs, promotion opportunities and earning better pay. Evidently, therefore, the two groups have diverse interests. The fact that the members in the general meeting have the statutory power to appoint and remove directors; decide the latter's remuneration and withdraw their funds from the enterprise, thereby having the potential to influence directors in their decision making, further confirms this point. Thus, although directors are not *legally* mandated to consider *only* the interests of shareholders, the latter group has been statutorily armed to ensure that the directors do just that. Conclusively, the legal power of shareholders to vote for the board of directors and their remuneration helps to perpetuate the shareholder primacy norm.[55]

Although both laws have made some provision for the company's employees as stakeholders so that the issue of their welfare is included in the directors' report, and they may share in the company's profit and can even possibly be compensated upon cessation or transfer of the business,[56] these provisions nowise make them equals with

[55] Refer to **3.4.2** supra on "In whose Interests and for whose Benefit should Directors Manage the Company?" for a recap on shareholder primacy norm.

[56] See ss.342(5), 384 and 566, CAMA respectively and ss.417(5)(b), 247, 549(2)(a) and 1166 CA. In particular, s. 566 CAMA and s.247 CA essentially reject the decision in *Parke vs. Daily News Ltd.* (1962) Ch. 927, wherein the court held that the defendant company had no power to make redundancy payments to its employees.

members in the company because of the critical issue of the absence of voting power. In the absence of *equality*, therefore, there is *primacy* to the advantage of the members, under the two laws.

Conclusively, therefore, the list of factors in s.172 CA is unlikely to change things. The effect of the section is more likely to be educational, rather than in any sense restrictive and so business decisions taken in good faith will not be any more easily challengeable than they were before the provision existed.[57]The provision is at best a modest development of the common law,[58] highly unlikely to have any great impact on company boards and how they transact business.[59]The fact that only the members among the list of stakeholders have the potential to enforce the duties of directors, further underscores this proposition. As well, placing members and employees in the same category as entitled to the special attention of directors, is misleading. On this point, s.172 CA is hardly any different from s.279(3) and (4) of the CAMA. Even the requirement for a business review under s.417 CA does not do much because the members are the likely recipients of that report and they are unlikely to raise any issues, unless their own interests have been jeopardized.

This writer puts forth the proposition that the various stakeholders of the company can more appropriately have their interests addressed outside of corporate law. Contract, torts, labour, tax, consumer and environmental laws present great avenues for addressing the interests of the company's respective stakeholders. Where these are inadequate, there may be a need for the laws to be reviewed. But importantly, the stakeholders would not here be faced with the kind of impediment they would encounter

[57]Birds, J., et al. (2011).*Boyle and Birds' Company Law.*8th edition, Jordan Publishing Limited, Bristol, p. 638.
[58]Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 543.
[59]Keay, A. (2010)*The Duty to Promote the Success of the Company: Is it Fit for Purpose?* Working Paper, Centre for Business Law and Practice, School of Law, University of Leeds, England, p. 36.Retrieved October 21, 2013 fromhttp://papers.ssrn.com/sol3/papers.cfm?abstract_id=1662411.

when attempting to safeguard their interests under corporate law, nor would the state on their behalf.

Perhaps, if the law had merely *permitted*, or *encouraged* the director to regard these varying interests, it would not have been so far off the track. But the fact that the law mandates the director to do so, is the contention here. A fortiori, it is not the place of law to instruct directors on the interests they must consider in their decisions. As Hollignton poignantly pointed out, this is the province of business schools and corporate codes of ethics.[60] Every business decision is based on certain peculiarities, such as the status, credit base, objective, success rate, and the general circumstance of a company. These vary for every company in every circumstance. This proves the futility of corporate law attempting to restrict the areas for a director's consideration.

Creditors, on the other hand, are a unique class in that they have direct investments in the corporation. S.172(3) CA simply confirms the long-developed common law rule that, under certain circumstances not mentioned under the subsection, the interests of the company's creditors take precedence over those of members or any other group. It is regretful that the law does not specify those circumstances in order to clarify them. However, they usually come up when the company is approaching insolvency. The Insolvency Act 1986 supports the CA on this. The CAMA has no similar special provision for creditors, nor alternative legislation, although many sections within the Act recognize the rights of creditors, particularly on wrongful trading and at winding up. It is submitted that in the interest of clarity, both laws ought to clarify the instances where the creditors' interests should be considered paramount.

Finally, on the point of the director's state of mind, s.172 CA requires him to reach his decisions in *good faith*, while s.279(3) CAMA requires him to act, not only

[60]Hollington R. op.cit.at p.7.

faithfully, but in a diligent, careful and ordinarily skilful manner, as well. Both sections border substantially on the director's *fiduciary* duty. Apparently, however, the CAMA provision has brought the director's duty of care and skill into it, in spite of the fact that s.282 chiefly addresses this. It is submitted that the law on this point as stated under the CAMA, is repetitive and ambiguous, even if it was thus enacted so as to emphasize the director's duty to show care and skill. This is because the director's duty of care and skill and his fiduciary duties of loyalty and good faith under the CAMA, are measurable by different standards: subjective in the former and objective in the latter. Thus, the law here requires clarification.

5.3.3 Duty to Exercise Independent Judgment

This duty replaces the common law rule against the director fettering his discretion to vote in a particular manner. The principle is widened under s.173 CA to require the director to "exercise independent judgment," thus encompassing judgment in any form, during the course of serving the company. Importantly, the section has clarified instances where the duty will not be infringed. Thus, where the director acts (a) in accordance with an agreement duly entered into by the company that restricts the future exercise of discretion by its directors, or (b) in a way authorised by the company's constitution, this duty will not be said to be infringed.

The drafters intended the CA to accommodate and reflect modern business exigency. Thus, the decision in **Cabra Estates Plc. vs. Fulham Football Club**,[61] has been codified here, in order to allow companies the freedom to contract in a manner fettering their discretions regarding future obligations. Importantly also, the constitution may specify certain exceptions to the rule regarding exercise of discretion by the

[61](1994) 1 BCLC 363, CA, following the Australian court's decision in *Thorby vs. Goldberg* (1964) 112 CLR, 597, Aust.HC.

director. It has also been suggested[62] that the duty as codified allows the director to freely seek professional advice and act on it, in order to achieve an informed judgment.

In contrast, s.279(6) CAMA simply codifies the common law rule that restricts the observance of the duty to voting situations. "Vote" is rather restrictive. It is submitted that it is not only when it comes to voting that a director's independence may be called to question. This is because a director's services to the company may go beyond voting at board meetings. Clearly, "independent judgment" is more all-encompassing than "discretion to vote." Further, the law as codified admits of no derogation from the tone used: "a director shall not fetter his discretion to vote in a particular way." This is further reinforced by s.279(8) CAMA which nullifies any provisions of the company's articles, resolutions or contracts with the director, which purport to qualify this duty in any way. This implies that, under the CAMA, a director cannot contract on behalf of his company to bind himself to act in a future manner, even in the company's own interests. This is in stark contrast to s.173(2) CA.

Evidently, s.279(6) & (8) of CAMA needs reconsidering in view of the fact that it does not support modern business exigency. Recall that companies have the capacity of natural persons in most respects. When it comes to contracting with others, there may be situations where a company would be required to conform to a contracting party's terms, such as in loan agreements, for example, or contracts involving patent rights. Perhaps, the only sensible qualifier to this rule would be an instance where some other law has clearly criminalized fettering of discretion in a particular manner, such as anti-

[62]Goldsmith MP of the Lords Grand Committee.See *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 9, quoting the Hansard of February 6, 2006, column 282, accessible at http://www.berr.gov.uk/files/file40139.pdf, and Davies, L.P. and Worthington, S. (2012). Op.cit. p. 536;

trust laws or conducts amounting to collusive practices, as was the case in **Shepherd vs. Williamson**[63]discussed earlier.[64] This is in order to allow for fair trading.

5.3.4 Duty to Exercise Reasonable Care, Skill and Diligence

This is another area where the UK law codified the common law that had developed up to the time of the enactment of the CA. Hitherto, the standard of care required was at best minimal for a director was not easily found liable when judged against that standard.[65] The general view then was that the common law gave directors a remarkable freedom to run companies incompetently.[66] Over time, however, the courts had a rethink[67] and s.174 CA was an attempt to set the record straight. Thus,

> *(1) A director of a company must exercise reasonable care, skill and diligence.*
> *(2) This means the care, skill and diligence that would be exercised by a reasonably diligent person with—*
> *(a) 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, and*
> *(b) the general knowledge, skill and experience that the director has.*

The section is reminiscent of s.214 of the UK Insolvency Act 1986. The law has effectively classified directors here because s.174(2)(a) CA takes into consideration the particular responsibilities attached to the office of any particular director, while subsection (2)(b) holds the director accountable to the extent of any extra qualifications he might possess. This makes the requirement cumulative.[68] Previously, the director's

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[63] (2010) EWHC 2375, Ch.
[64] Refer to **4.2.3** supra.
[65] See for example the cases of *Re City Equitable Fire Insurance Co.*(1925) Ch. 40; *Re Cardiff Savings Bank (Marquis of Bute's Case)* (1892) Ch. 100 and *Re Brazilian Rubber Plantations and Estate*(1911) 1 Ch. 425.
[66]Finch, V. (1992).Company Directors: Who Cares About Skill and Care? *Modern Law Report,* 55 (2): 179 at 179.
[67] Beginning with cases such as *Dorchester Finance Co. Ltd. vs. Stebbing,* decided in 1977, but reported much later: (1989) BCLC 498; *Norman vs. Theodore Goddard* (1991) BCLC 1028; *Re D'Jan of London Ltd.* (1993) BCC 646; and *Re Barings Plc.* [No. 5] (2000) 1 BCLC 523.
[68]Goldsmith MP of the Lords Grand Committee.See *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 10,

subjective level of skill set the standard required of that director, whereas under s. 174, the director's subjective level does so only if it improves upon the objective standard of the reasonable director.[69]

Thus, the law has clearly not simply lumped all directors into one category and expects them to display the same standard of care and skill. For this reason, it is submitted that the rule is fair. Although "reasonable" is a highly nebulous term, the decision in **Abbey Forwarding Limited (in liquidation) vs. Hone**,[70] indicates that, in deciding any case, evidence of what is normal in the field of commerce in which the company operates, is relevant.

In the case of the CAMA, s.282 simply expects every company director—no matter the type of responsibilities attached to his office, or his personal qualifications—to measure up to reasonable standards.S. 282(1), provides that "every director of a company shall...exercise that degree of care, diligence and skill which a reasonably prudent director would exercise in comparable circumstances." There is no allowance here for consideration of office or personal qualification, barring any special terms in any service contract between the director and the company. Thus, where a director possesses more skills than the reasonable man, he would still only be judged by the latter's standards. Recall that the director is generally the agent of the company. Therefore, the company is entitled to the very best of services the director can offer. Thus, s. 282 of the CAMA would appear to be a bit generous on the 'skilful' director.The disadvantage of this rule compared to s.174 CA is obvious and can be summarized thus:

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quoting the Hansard of February 6, 2006, column 284. Retrieved March 10, 2013, from http://www.berr.gov.uk/files/file40139.pdf.

[69]Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 520.

[70](2010) EWHC 2029 (Ch).cited in Bills Committee on Companies Bill: Follow-up to the Meetings on 3 and 10 June 2011 Supplementary Information (June 22, 2011). Financial Services and the treasury Bureau, Companies Registry, p. 8.Retrieved December 11, 2013, from http://www.legco.gov.hk/yr10-11/english/bc/bc03/papers/bc030628cb1-2577-1-e.pdf.

1. if a director happens to have more qualification than reasonably necessary, he would still only be judged by the reasonability standards;
2. the standard does not take into consideration a particular director's position within that type of company; and
3. it unfairly categorizes all directors into the same category, when this is hardly ever the case in reality.

But s. 174 CA takes all these into consideration, while still maintaining a minimum reasonable standard below which no director is allowed to go. And it is submitted that subjecting the more qualified director to a higher standard is fair. At least, it would discourage prospective directors from embellishing their resumes and companies would be sure they are getting exactly what they bargained for. The argument that the rule might discourage highly qualified persons from opting for the office is unfounded, since such persons can use this to their advantage to bargain for better pay, for which they know they are prepared to deliver. Recall also that s.174 CA is further supported by the Company Directors Disqualification Act 1986 and the Insolvency Act 2000, which combine to disqualify persons found liable for misconduct, such as breach of the duty under s.174, from being involved in the formation or management of companies and, in particular, from being company directors, in the future.[71]

In spite of the differences noted in the standard of care required, the two laws still share something in common. Prima facie, all directors must measure up to reasonable standards in both legislations. On the issue of delegation, the CA apparently does not change the common law rule that, though a director may delegate,[72] he must still supervise the discharge of the delegated function.[73]S.279(7) CAMA also clearly allows delegation, though it sounds a caution against delegating in a manner that may

[71] See in particular ss.6 &11 of the Company Directors Disqualification Act.
[72] Application of which rule would be consistent with s. 170(3) and (4) which acknowledge the continued application of common law principles consistent with the Act.
[73] *Re Barings Plc.* [No.5] (2000) 1 B.C.L.C. 433.

amount to an abdication of duty. The consequences for breach are also the same:basically an action for negligence and breach of duty.

There is some truth to the view held by Justice Arden[74] that courts now, unlike before, appreciate that in large, modern corporations, there's a distinction between oversight and management so that the nature and extent of the duty of skill, care and diligence will depend on such factors as the size, location and complexity of a company's business and the urgency of any decision because other jurisdictions, such as Australia,[75] Hong Kong[76] and South Africa,[77] have sections similar to that in the CA on the standard of conduct required of a company director. Conclusively, s.174 CA has much to commend it.

The standard of care required of directors is gradually tightening up, from the days of **Re City** when they were purely subjective, to the uniform objective standard and now to a cumulative objective/subjective standard. This is a sign of the times. Nowadays, directors often have one or more qualification. The view of corporate law now is that it does not matter their qualification, but they must discharge their duties while exercising skill and care up to a reasonable standard and, where they have held themselves out as experts or otherwise, up to that additional standard.

Besides, we live in an era of rising standards of commercial education which justifies the rise in expectations regarding the level of care and expertise to be displayed by directors. With rising unemployment, it would beunreasonable to argue that a rise in standard of care is likely to discourage business men from accepting such positions. It is also not a plausible argument to hold forth that the added subjective standard would likely discourage directors from seeking to improve their own level of skill because

[74] See Arden, D.B.E., op.cit. at 169.
[75] See s. 180(1) Australia Corporations Act 2001 (as amended).
[76] See s. 465 of the new Hong Kong Companies Ordinance 2012.
[77] See s. 76(3)(c) of the South African Companies Act 2008.

directors do not normally receive the same pay and more often receive pay based on the level of their qualifications and expertise. The prospect of receiving better pay with higher qualification is incentive enough for directors to seek to improve their level of expertise.

5.3.5 Duty to Avoid Conflicts of Interest

This rule was strict under the common law: "no man can…acting as an agent, be allowed to put himself in a position in which his interest and duty will be in conflict."[78] Otherwise, he would be liable to pay over all the profits to his principal. The law under s.175 CA prima facie observes the common law rule, but further qualifies it with an exception which recognizes authorization by the board of directors. The rule does not depend on fraud, or absence of bona fides; or upon such other similar considerations.[79] With respect to directors, this rule applies because they are presumably trustees of the company's information, property and opportunity. S.175 CA[80] requires a director to avoid situational conflicts, direct or indirect; actual or possible, and rightly excludes transactional conflicts from its ambit. The question whether an actual or potential conflict of interest has arisen, is one for the courts.[81]

Under the CAMA, s.279(1) considers company directors to be fiduciaries of the company, so that they must observe the utmost good faith in any transactions with it or on its behalf. S.283 particularly regards them as trustees of its properties. Thus, s.280(2)(b) forbids them from making any gains from the company's property, while doing their duty. There are lacunae and grammatical ambiguities in the statement of the duty under this head. In the first place, the demand that a director should observe good faith in any transactions *on behalf of* the company is quite justified, considering the

[78] Per Lord Cairns in *Parker vs. McKenna* (1874) 10 Ch. App. 96.
[79] Per Lord Russell in *Regal (Hastings) Ltd. vs. Gulliver* (1967) 2 A.C. 134, at 144-145.
[80] Please refer to Appendix A.
[81] Davies, P. and Worthington, S. (2012). Op.cit. at 591.

director's powers and status under the law. But requiring him to observe "utmost good faith" even in transactions *with* the company, it is submitted, is quite misleading, considering human nature.[82] Indeed, Lord Cranworth's remark that such situations would lead the director in a direction opposite the interests of the company, towards his own interests, rings true.[83] A director dealing with the company would more likely be watching out for his own benefit and interests and seek to make the best bargain for himself, rather than for the company. Besides, the law allows the director to transact with the company qua a third party and not qua its director.[84] Thus, the law has, perhaps inadvertently, been misstated in s.279(1).

CAMA in s.280 uses the language "shall not" in a statement in which it requires the director to refrain from or avoid a particular action, rather than the more appropriate "must not."[85] The latter phrase is the more modern English in describing obligations. Furthermore, s.280(1) is stated in general terms and neglects to clearly identify the situation(s) of conflict alluded to, or at least, recognize the exception in situations of transactions or contracts with the company, already admitted by s.277 CAMA. Ss. 280(2) and (3) also use the vague and nebulous term "unnecessary benefit" which does not adequately describe to the director the kind of gain or profit which he must resist but even appears to allow his subjective judgment as to what is 'unnecessary' or 'necessary'. Further, s. 280(5) and (6) respectively refer to "the duty not to misuse corporate information" and "the transaction", neither of which terms has been previously discussed earlier in the section, so that the use of the definite article "the" is misleading.

Considering the foregoing, s.175 CA has many advantages over s.280 CAMA, including clarity. In the first place, s.175(1) contemplates both actual and possible, as

[82] See the observation of Lord Cranworth supra in*Aberdeen Railway Co. vs. Blaikie Bros* (1854) 23 LTR 315 at 316.
[83]See *Aberdeen Railway Co. vs. Blaikie Bros* (1854) 23 LTR 315 at 316.
[84] See s.277 CAMA for example.
[85] Refer to **1.1** supra on this note.

well as direct and indirect conflict situations, and the reasonability doctrine is admissible to determine breach in each particular case.[86] The company's interests to which the rule applies has also been adequately described as information, property and opportunity. Furthermore, the section has clarified the exceptions to the rule with respect to transactions with the company, since the CA allows this, as well as states instances when the rule would not be said to have been infringed. Finally, the mode of disclosure and authorization is detailed.

However, there are common grounds discernible from both legislations under consideration. First, both laws consider it immaterial in determining liability, that the company at the relevant time could not in fact have utilized the property.[87] Second, the duty covers conflict of duties as well, so as to also apply in situations of multiple directorships.[88] Finally and more importantly also, the duty, with respect at least to information in the case of the CAMA, is considered to continue even beyond the resignation of the director, so that he may not resign in order to take advantage of the company's interests.[89] Why this is not the case with respect to property and opportunity as well, is not clear. This is probably an oversight on the part of the drafters of the CAMA, considering the spirit of the law regarding prohibition of conflicts of interests, contemplates prohibition of any profit or gain from such cases.

In spite of the areas of convergence discussed above, the laws differ substantially in the default authorizing body. The authorisation regime is one of the areas reviewed by the CA from the former common law position.Formerly, the common law did not condone authorisation of conflicts of interest situations by the board, insisting always on

[86] Lord Goldsmith of the Lords Grand Committee, reported in the Hansard of May 9, 2006, column 864. Cited in: *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 13, per, accessible at http://www.berr.gov.uk/files/file40139.pdf.
[87] See s.175(2) CA and s.280(4) CAMA.
[88] See s.175(7) CA and s.281 CAMA.
[89] See s.170(2)(a) CA and s.280(5) CAMA.

the general meeting as the proper body to act instead.[90] However, even the interested director, if he happened to be a shareholder, could participate in the authorisation process and vote.[91] This is the position held by CAMA from the tenor of s.280(6). Unlike s.180(4)(b) CA, the CAMA does not specifically allow the articles to make provisions for dealing with conflicts of interests.

Apparently, the drafters of the CA did not intend to outrightly prohibit conflicts—a task considered impossible, considering human nature—but simply to allow companies, particularly the board of directors, to decide whether or not to allow a director take advantage of the company's interests in the form of information, property or opportunity in any given case. In suggesting the contents of s.175, the CLRSG may have been persuaded by court decisions such as those in **Peso Silver Mines Ltd. vs. Cropper,**[92]**Queensland Mines Ltd. vs. Hudson,**[93]and **Foster vs. Bryant**,[94] discussed supra,[95] which tend towards a softening of the rule, for it recommended making authorisation easier for interested directors.

The CLRSG considered the previous framework regarding personal exploitation of corporate opportunities impractical, due to the requirement for member approval in all cases, so that the framework was said to be "unduly strict" and "inconsistent with the principle that it is for the board to make business assessments and stifles entrepreneurship."[96] It therefore proposed, and Parliament accepted, that statute should

[90]*Benson vs. Heathorn* (1842) 1 Y. & C.C.C. 326; *Imperial Mercantile Credit Association vs. Coleman* (1871) L.R. 6 Ch. App. 558, C.A.; *Regal (Hastings) Ltd. vs. Gulliver* (1967) 2 A.C. 134.
[91] See *North-West Transportation Co. Ltd. vs. Beatty* (1887) 12 App. Cas 589; *Northern Counties Securities Ltd. vs. Jackson and Steeple Ltd*. (1974) 1 WLR 1133 at 1144, 1146; *Estmaco Ltd. vs. Greater London Council* (1982) 1 All ER 437 at 444.
[92](1966) 58 DLR (2d.) 1.
[93](1977) 18 ALR 1.
[94] (2007) Bus LR 1565.
[95] Refer to **4.2.6** supra.
[96] Company Law Review Steering Group, *Modern Company Law for a Competitive Economy: The Final Report*, Volume 1, London, DTI, 2001, p. 46

allow the company's rights to be waived by a disinterested board.[97]In fact, the idea behind the content of s.175 is actually to *allow* conflicts, provided there is disclosure and authorisation, and provided also that there are no provisions within the articles inconsistent with this board power.[98] Thus, changes were made in order to facilitate the exploitation of corporate opportunities "which might otherwise be left to waste because of the expense of convening a general meeting."[99]It is considered a stifling of enterprise and impediment to free competition, to keep directorsbound by their loyalty to the company regarding opportunities already rejected by their companies, where the rejection was bona fide. Hence, for private companies, the default ruleunder the CA is that a disinterested or non-conflicted board may consider proposals on such conflicts and decide whether or not to authorise them, provided there are no provisions within the articles inconsistent with this board power.[100] As for public companies, the articles are required to have enabling provisions empoweringthe board to consider and authorise any such conflicts.[101]

The drafters are of the view that the requirement for the authorizing board to be disinterested and the fact that the disinterested directors are still held to their duty to act in good faith in a way most likely to promote the success of the company, will work to ensure that the authorization policy is not abused.[102]However, as observed earlier in this work,[103] there are risks attendant with this authorization policy. Granted, the board is

[97] Refer to s.175(5)(a)&(b) and (6)(a)&(b) CA.
[98]Per Lord Goldsmith of the Lords Grand Committee.*Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 11, quoting from the Committee Report in the Hansard of 6th February 2006, column 288.Retrieved December 23rd 2013, from http://www.berr.gov.uk/files/file40139.pdf.
[99]Arden, D.B.E., op.cit. at 169.
[100] See ss.5(a) and 6(a) and (b) CA.
[101] See ss.5(b) and 6(a) and (b) CA.
[102]Per Lord Goldsmith of the Lords Grand Committee.*Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007) p. 11, quoting from the Committee Report in the Hansard of 9th February 2006, column 327.Retrieved December 23rd 2013, from http://www.berr.gov.uk/files/file40139.pdf.
[103] Refer to **4.2.6** supra.

ideally the most appropriate organ to decide matters regarding the exploitation of its property, etc. Still, board authorization has the potential to invite boardroom mischief by encouraging 'backscratching' among board members.[104]Thus, directors, even abstaining or absent, can still influence board decisions.[105] Again, directors may not be encouraged to do their best to secure the company's interests if they know they can conveniently "release" the company's opportunity for their future use. Besides, how can the company be certain that the rejection of an opportunity, etc was bona fide in each case? A fortiori, it would be dangerous to allow the board to delineate the scope of board members fiduciary duties: essentially allowing directors to be judges in their own cause.[106] Moreover, the argument about the expense of convening general meetings is not so persuasive because conflicts of such nature are unlikely to be frequent enough to justify that view.

For these reasons, the default rule in s.175(5) CA has the tendency to encourage breach, or at the most, is more suited for private companies, where the demarcation between management and members is often blurred. It is therefore submitted that the common law rule on authorisation reflected in s.280(6) CAMA is better suited to guard against abuse.[107] Perhaps, it may be that a conflicting director who happens to be a member would be able to vote towards his interests. But the fact is that shareholders, unlike directors, are not subject to fiduciary duties.[108] For this reason, their shares and the attendant rights, are to be regarded as their property, with all the inherent rights to use them in their own interests. For balance, the law allocates to the minority certain avenues through derivative action by which they may get redress from any oppressive tendencies of the majority.

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[104] See Davies, L.P. and Worthington, S. op.cit. at p.602.
[105] seeCorkery, F.J. (1987).*Directors' Powers and Duties*. Longman Cheshire, Melbourne Australia, p.87.
[106] Ibid. at p.88.
[107] Or at least, the lesser of the two evils.
[108] Davies, L.P. and Worthington, S. op.cit.at p.622.

5.3.6 Duty Not to Accept Benefits from Third Parties

This duty is another aspect of the general rule against conflicts of interests discussed above. S.176(1) CA provides that "A director of a company must not accept a benefit from a third party conferred by reason of—(a) his being a director, or (b) his doing (or not doing) anything as director." Though the provision makes no direct mention of it, the law clearly contemplates bribes within the prohibition, thereby complementing the UK Bribery Act 2010. Importantly, the drafters intend "benefit" to admit a wide interpretationincluding non-financial gains, gifts and other such advantages,[109] and they need not even be 'secret', from the tenor of the section. Where the benefit is in the form of corporate property or information, the rule discussed in s.175 may also apply, since s.179 CA recognizes that one or more of the general duties may apply in any particular case.

Furthermore, the section does not only define "third party"[110] but also clarifies situations that would not be regarded as a breach of the duty.[111] Thus, the duty is not infringed where the gift is given by the director's nominator to the nominee director, nor where the acceptance of the benefit cannot reasonably be regarded as likely to give rise to a conflict of interest. This effectively allows the courts to decide breach cases based on reasonability. Thus, the question of the director's good faith does not arise in these matters.

Under the CAMA, ss.280 and 287 appear to be closely related:[112] it is curious that the sections do not follow each other. While s.280 generally prohibits secret profits and benefit, s.287 of the law further prohibits a director from accepting a bribe, a gift, or

[109] Per Lord Goldsmith of the Lords Grand Committee at the Committee hearing on 9 February, 2006. See Hansard, Column 330. *Companies Act 2006: Duties of Company Directors*, Ministerial Statements published by the Department of Trade and Industry (DTI), (June 2007), p. 12, accessible at http://www.berr.gov.uk/files/file40139.pdf.

[110] See s.176(2) CA.

[111] See s.176(3) and (4) CA.

[112] See **3.8** supra on Duty Not to Accept Secret Benefits.

commission either in cash or kind, from any person, or sharing in the profit of that person in respect of any transaction involving his company in order to introduce his company to deal with such a person. Clearly, the drafters intended "introduce" to read "induce" in the latter section. Otherwise, the wording would not make sense. S. 287(2) clarifies the consequence of breach as disgorgement, in addition to damages. Also, the law recognizes an exception to the rule in cases where unsolicited gift is offered as a sign of gratitude after the transaction. However, a declaration must be made before the board and the fact must be recorded in the minutes book.

The two laws share little in common, apart from the fact that both clearly admit bribery within the prohibition. Also, secrecy is not a factor considered in determining liability under either s.176 CA or s.287 CAMA. Although the marginal notes in s.287 CAMA refer to "prohibition of secret benefits," the term "secret" features only in the last subsection. Obviously, it would not matter that the gift/benefit was "openly" received.[113]

The provisions of the two laws differ in certain respects regarding the duty under review. Firstly, where s.287 CAMA prohibits the taking of bribe, gift or commission in cash or kind, s.176 simply prohibits benefits, which word, it is submitted, neatly encompasses all the items mentioned under s.287(1) CAMA and admits more. Secondly, the tenor of s.287(1) CAMA appears to restrict the application of the rule to the motive of inducement. That is, cases where the director accepted the bribe, gift or commission in order to induce his company to deal with such a person. Thus, where the gift or commission is received by the director without any evidence of corrupt motive or where it is apparent that the director was actually unaffected, the rule under the section would not apply. But this would not be the case under s.176 CA which appears to leave

[113] However, compare situations falling under s.280 CAMA which clearly refer to secret profit.

no loophole, since the rule applies even where the benefit was given simply for being a director of a particular company. The idea behind the principle under discussion is to prohibit unauthorized profits or gains in the course of discharge of the duties attached to the office. Thus, there is no room for the director's subjective judgment in these cases.

Thirdly, where s.176 CA speaks of "third party" and defines it, s.278 CAMA mentions "any person" and does not define it. Potentially, an associated corporate body or person acting on its behalf can come within the meaning of "any person", which may not have been the intendment of the drafters. Fourthly, where s.176(3) CA makes concessions regarding benefits received by nominee directors from their nominators, s.278(3) CAMA on the other hand makes concessions regarding unsolicited gifts received as a sign of gratitude after the transaction.

Fifthly, s.176(4) CA intends the reasonability doctrine to apply in determining liability under the rule, while s.287(4) disregards the fact of any benefit to the company or the good faith of the director as defence to a breach of the duty. It may be that this will practically lead to the same results. This is because, if the good faith of the director is disregarded, the implication is that a subjective test is discarded for an objective, reasonable standard in determining liability. However, the issue of benefit to the company is entirely a different matter.

Finally, s.170(2)(b) CA clearly imposes the duty in s.176 on a former director, as it does on a substantive. This would discourage a director from resigning simply to take advantage of what was offered. The CAMA provision does not contemplate such a situation, perhaps because of the difficulty a company might encounter regarding proof. However, it is submitted that, if the company can—and it is possible that in clear, obvious cases, this would be easy—it should have the right to go after a former director

for any such benefits he receives in contravention of that duty. After all, this is an extension of the duty to avoid conflict of interests, for which a similar rule applies.

It is pertinent to note also that, by virtue of s.176(5) CA, the rule therein also covers conflict of interest and duty and conflict of duties situations. Thus, a multiple director is bound by the duty as regards any benefit he may gain for one company that would be in breach of the duty he owes another company under s.176 CA.

The exception recognized in the case of unsolicited gift under the CAMA needs further consideration. It has the potential to lead to abuse of opportunity by a director, where he connives with the third party so that it appears that the gift was offered after the transaction and was unsolicited. Short of a confession from the third party, a company would have no way of ascertaining that this was in fact the case.

With respect to the use of the term "benefit" and "third party" as defined, s.176 CA is clearer. Also, the concept of reasonability introduced under subsection (4) is helpful in properly determining liability and lending practical tone to the provision, so that it would not be unduly harsh or impossible. For example, in the course of negotiating a contract with a third party on behalf of the company, a director who accepts a pen from the third party, with which he signs the document, cannot reasonably be said to have breached the duty not to accept benefit from a third party. Most importantly, the main head of the duty as provided under subsection (1) has been cleverly drafted to leave hardly any escape route for a dubious director. However, with respect to the rule regarding nominee directors and their nominators under the CA, the law may have been too accommodating in that case. The point is, every director's duty is first and foremost to the company, not his nominator. Otherwise, if his nominator were to use benefits and favours in order to be so controlling over him, the nominator could qualify as a shadow director. Besides, if the nominee does his duty to the

company, any success the company achieves would eventually rub off on the nominator. Thus, allowing conflicts in this case may potentially lead to abuse of power.

5.3.7 Duty to Declare Interest in Proposed or Existing Transaction or Arrangement

Company law does not prohibitconflicts of interest arising from the fact of a director having any form of transactions or arrangements with the company. Recall that though a director is a fiduciary, his fiduciary status has been described as *sui generis* especially because the characteristics typically attributable to the offices of trustee and agent do not normally apply to him.[114] For instance, though a trustee of the company's powers and assets, the company director may still transact with the company, thereby temporarily keeping his "good faith" for the company aside. Consequently, the law allows him to occasionally wear two hats, unlike the typical trustee.

Under common law, the director was for some time, completely precluded from transacting with the company.[115] But it was realized that an outright ban may not be good for business in certain situations. Thus eventually, the critical issue came to be identifying the proper procedure to be observed in order to rid the director of the taint of conflicted contracting while allowing him to so contract, rather than an outright prohibition. Thus in time, the rule came to be that the director could escape liability only by disclosing the conflict in advance to, and obtaining the approval of, the members.[116]

The CA has substantially clarified the law in this area, first, by distinguishing the rule on "proposed" transactions from that on "existing" transactions. For proposed transactions or arrangements, s.177 CA mandates thatthe director must declare the

[114] Refer generally to **2.6** supra on Status of Directors.
[115] *Aberdeen Railway Co. vs. Blaikie Bros* (1854) 23 LTR 315.
[116] *North-West Trans. Co. vs. Beatty* (1887) 12 App. Cas. 589. See further Davies, L.P. and Worthington, S.op.cit. at p. 562 andCorkery, F.J. op.cit., at p.79.

nature and extent of his interest to the other directors. Further, the law acknowledges "indirect" interests as coming within the rule in order to discourage a director from effectively breaching the rule through his family members or business associates. "Interest" has not been defined, though the transaction must reasonably be regarded as one likely to give rise to a conflict of interest and not a mere possibility of conflict, as earlier contemplated under the common law.[117]

The kind of dealing contemplated is "any proposed transaction or arrangement." Thus, every kind of contract, from the simplest to the most complex, is here accommodated, although "proposed" indicates that the transaction/arrangement is merely being contemplated and not yet concluded: disclosure here is required pre- and not post-contract. The law also requires the disclosure of both the nature as well as extent of the director's interest.

Significantly, the disclosure regime under the common law no longer applies, as s.177 CA requires disclosure simply to "the other directors," even though the articles may impose additional requirements, such as additional disclosure to, or approval of, the general meeting. Here, the board to which disclosure is to be made is not required to be "disinterested" as is the case under s.175. Again, one obvious conclusion from s.177 is that it does not contemplate disclosure where there happens to be only one director,[118]since there would be no "other" in that case, to whom to disclose. Conclusively, the sole director of a private limited company is not bound by the duty under s.177.[119]

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[117]See the statements by Lord Cranworth L.C. in *Aberdeen Rly. Co. vs. Blaikie Bros* (1854) 23 LTR 315 at 325 and Sir Richard Bagallay in *North-West Trans Co. vs. Beatty* (1887) 12 App. Cas. 589 at 593, from the earliest cases.

[118] Under the new Companies Act, a private company need not have more than one director. See s.154(1) CA.

[119]However, s.231 CA requires the sole director to set down the terms of any contract in writing or record them in the minutes of directors' meeting, where he happens to contract with the company while being its only member.

Further, s.177 has not only suggested a choice of means for disclosure, but has also identified circumstances where disclosure would not be required. Thus, the directors are treated as aware of everything they ought reasonably to be aware of, in connection with the conflicting director's interests. On the part of the conflicting director, the law effectively rules out ignorance as a defence to a breach of the duty under s.177, by treating the director as aware of matters of which he ought reasonably to be aware of. Thus, he cannot be 'unreasonably unaware' of his interests and thereby fail to disclose them. A fortiori, when disclosurebecomes inadequate, after having been made, a further disclosure is required.

As for existing transactions, a director who is interested must disclose such interest in the same manner as under s.177 CA, as soon as the director discovers that he has such interests.[120] However there are two important differences in the rules relating to existing and proposed transactions. Firstly, shadow directors are specifically required to disclose interests in existing, though not proposed, transactions. Secondly, liability for breach in the case of existing transactions is criminal,[121] while that for proposed transactions is civil, as was previously the case under common law.[122]

Under the CAMA, s.277 combines the duties separately captured under ss. 177 and 182 of the CA. The rules in both legislations are the same to the extent that both the CA and the CAMA address direct and indirect interests; require disclosure to the board and allow disclosure at the meeting of directors or by tendering general notice.[123] However, while CA talks of 'transaction or arrangement,' the CAMA talks of 'contract.' There appears to be hardly any substantial difference between the two

[120] See s.182 CA.
[121] See s.183 CA.
[122] See s.178(1) CA.
[123] See s.177(1) and (2) CA and s.277(1) and (3) CAMA

terminologies. Indeed, it is hard to fathom a transaction or arrangement between a company and another, which would not, in some way, fit the description of 'contract.'

However, there are considerable differences discernible from both legislations. First, s.177(1) CA requires the declaration of both nature and extent of interest, whereas s.277(1) CAMA requires simply the declaration of nature of interest. Thus, under the CAMA, it would be enough to simply state, "I am a shareholder in ZT Ltd" or "My wife is associated with No. 54, Kaduna street, Sabon-Gari, Zaria," not necessarily, "I own 1% of the shares in ZT Ltd." or "My wife's family owns No.54 Kaduna Street, Sabon-Gari, Zaria." Clearly, there is a world of difference between the first set of statements and the second. The latter would allow the board to easily reach a more informed decision about the issue.

Second, under s.177(2) CA, declaration need not be via the mentioned means (i.e., at a meeting of directors, by notice in writing or general notice). It can be through any other means that can effectively bring the fact of the director's interests to the notice of the others. While it is hard to think of any other means apart from the aforementioned through which the director can effectively deliver the message, it is still submitted that leaving it open to the director to seek any means easy to him is commendable because this would have the potential to deny the director any excuse to say that he could not declare through the aforementioned means. He could call them up on phone, for example, especially where there are not many "other" directors. Thus, he would have no excuse.

Under s.277(2) and (3) CAMA on the other hand, declaration for proposed transactions or contracts, is either through notice given at the directors meeting or general notice. Considering the fact that information technology has improved considerably, notices via phone and emails should also be recognized or at least, the

provision can be left open, as is the case under s.177 CA, using the phrase, "need not be made," so that any other means not necessarily mentioned, but which could effectively transmit the notice, can be accommodated.

Third, under s.177(3) CA, the law requires a further declaration or update on the information earlier given, whenever the director involved discovers that the information given earlier has become inadequate or was at the time incomplete. This situation is not within the contemplation of s.277 CAMA. Thus, under the latter law, if the director declares the first time, he is not statutorily required to make a further declaration. This has the potential to allow dubious directors to make inadequate declaration in order to claim later that they had declared what, at the time, was known to them, or that they discovered the inadequacy (or the inadequacy occurred) much later, after the first declaration, and they were not obliged, thereafter, to make a further declaration.

Fourth, s. 177(5) and (6) CA have delineated instances where a declaration of interest would not be required,[124] which is not the case with the CAMA. The latter seems to admit of no exceptions to the rule. Therefore, under the CAMA, it would not be a defence for the director to state that he was not, at the time, aware of the interests in question or the particular contract; or that the interest cannot reasonably be regarded as likely to give rise to a conflict of interest; or that the interest is so notorious that the other directors are already aware of it; or that the interest concerns terms of his contract of service that has been, or is being considered by the company. It is submitted that these are valid defences, especially when the concept of reasonability is adopted in considering cases when the requirement for declaration is warranted. Therefore, a commendable feature of s.177 CA over s.277 CAMA is the recognition that a director is

[124] Which exceptions are supported by common law. See for example *Cowan de Groot Properties Ltd. vs. Eagle Trust Plc* (1991) BCLC 1045 on reasonable likelihood of conflict, and *Runciman vs. Walter Runciman Plc*. (1992) BCLC 1084 on interest concerning service contracts which have been, or are to be, considered by a meeting of directors or by a remuneration committee.

treated as being aware of matters of which he ought reasonably to be aware, so that where it would be unreasonable to suppose that the director is aware of a particular interest or transaction, the law would not 'unreasonably' find him in breach for not declaring. Again, where a transaction cannot reasonably be regarded as likely to give rise to a conflict of interest, such a declaration is not mandatory.

Finally, with respect to liability,the same criminal liability applies in both cases of proposed as well as existing contracts in the case of the CAMA, while under the CA, liability is civil in the case of proposed, and criminal in the case of existing transactions.It is not clear why this is the case. Perhaps it is because the option to rescind or avoid the contract would be less readily available to the company in the case of existing transactions. Thus, the fine imposed constitutes punishment. If this is the case, then the same rule should apply to proposed transactions as well because where a hefty fine is imposed, it would better discourage a director from keeping his interests in such cases secret. It is thus submitted that the approach of the CAMA on this point is better, although the fine imposed, N100, is utterly ridiculous today.

Obviously from the foregoing, apart from the matter of liability, s.177 CA is clearer and more practical in approach, in comparison with s.277 CAMA. However, with respect to disclosure, it is submitted that both laws are inadequate and need reviewing to prevent or discourage abuse of power and office by devious directors. Granted, disclosure whether or not to a disinterested board, would not make any difference, since it is simply a matter of receiving information to be used later. But what about the decision to be made following that disclosure? Both laws do not require the matter to be considered by a 'disinterested' board, especially with respect to proposed transactions. Hence, the interested director, together with his cronies and any persons connected with him, can sit to decide that the company would still go ahead with the

contract, in spite of the nature and extent of the directors' interests. It is thus submittedthat there ought to be included in the provisions of s.177CA and s.277 CAMA a statement to the effect that, although disclosure is to be made to the other directors, the board considering the transaction ought to be a disinterested one, and in the absence of such a disinterested board, the matter be referred to an informed general meeting.This will more effectively nip in the bud the undesirable practice which this particular principle of law seeks to address.

As for the related principle on substantial property transactions between a director and the company, both laws are similar.[125] The disclosure to, and approval of, the general meeting is required in such cases. Both laws also specifically include shadow directors and connected persons within the rule.[126]

[125] See ss.190-199 CA and ss.284-286 CAMA.
[126] See ss.190(1) and 187 CA and s.284(1) and (3) CAMA.

CHAPTER SIX

CONCLUSION, FINDINGS AND RECOMMENDATIONS

6.1 Summary

This work proceeded upon the premise that the Companies and Allied Matters Act 1990[1] (CAMA) is overdue for review and the UK Companies Act 2006 (CA) is a relatively up-to-date legislation which has codified more recent developments in case law and corporate practice. Nigeria having looked to the United Kingdom in drafting the CAMA and other laws previously, any attempt at reviewing the CAMA would most likely consider the CA as a foremost reference point.

Directors' duties of care and skill and fiduciary duties of loyalty and good faith as codified under the CAMA and the CA were each examined. The provisions under the CA stood out in that theyappeared more in tune with the latest court decisions and corporate practice. With respect to the provisions in the CAMA, apart from the grammatical errors observed, the law appeared not up to current standards with respect to the director's duty of care and skill, and absurd in its statement of the nature of the relationship between the director and the company. Interests of the company and members were not aligned. s.279 (2) and (4) appeared to imply that individual shareholders and employees are owed fiduciary duties whereas clearly, s.279(9) CAMA allows only the company to enforce these duties. On conflicts of interests and the rule on secret benefits, the CAMA had the common law principles poorly codified.

Under the CA, however, the main heads of duties were clearly spelt out and exceptions to the general rules were specified in each case so as to leave the director in no doubt as to circumstances in which he will not be unreasonably held liable for breach of a duty under the law. Instances have been provided where the company's articles can

[1] Cap C20, Laws of the Federation of Nigeria 2004.

modify some of the duties expected of its directors to observe. With respect, however, to decision making, it was found that the director's subjective judgment had been greatly encroached upon by the law, so that it appears he has a duty to consider a host of factors, which consideration would bepractically difficult to enforce against the director.

6.2 Conclusion

The provisions on directors' duties under the CAMA are not absolutely clear. Company law ought to be clear on such important matters, which go to the heart of corporate governance. The duties must therefore be clarified and simplified for corporate stakeholders and also reviewed from time to time, in tune with developments from case law and practice. A comprehensive amendment is required, preferably according to the UK CA, which appears to be a very good model. If the duties are made clearer, prospective company directors would better understand beforehand what they are up against and therefore, either decline positions they know they are incompetent to handle, or at the very least, resolve from the onset to put in their best.It may alsorevive corporate litigation which is currently almost non-existent in that area. A review in this area will substantially be in aid of, and promote, the culture of good corporate governance, which various regulatory agencies of corporate Nigeria are struggling to entrench.

6.3 Findings

After comparing the two laws under the particular heads of duties separately, the following findings were made:

1. **On the duty of care and skill**

The standard described under s.282 CAMA greatly improves from those required under the previous common law. But it can be better. It is not the best suited for today's business climate whereby directing comes with varieties of companies and positions within companies. Furthermore, directors today, whether executive or non executive,

present impressive resumes to their companies. Although the standard set by s.282 CAMA would require the incompetent director to perform up to the level of a notional director in the same situation, the provision has the potential to allow a director who is actually more competent than the notional director, to escape liability, unless there is a service contract between him and the company which requires him to exercise higher standards of skill and care. Non executive directors do not usually have service contracts. The dual objective/subjective liability threshold provided under s.174 CA, apart from considering 'reasonability' based on function and company type, has the further advantage of taking such situations into consideration, and is therefore, the more suited to the realities of the office of company director today.

2. On the duty to act in the best interests of the company

s.279(3) and (4) CAMA does not recognise the interests of the company as being inseparable from the interest of members. This has the potential to allow the director proceed on the erroneous belief that the two are distinguishable when in fact the courts have consistently held otherwise and the director will be left alone to decide the best interests of the company on his own terms, without any leverage on such a decision. The tenor of the law fails to recognise the fact that the corporation, though a legal personality, is in fact artificial and without any factual existence, so that its achievements, success or profits are ultimately for the use of natural persons who have set it up for profit. S. 172(1) is comparatively more in tune with reality in that it considers the success of the company to be achieved for the benefit of its members as a whole. As for matters to which the director may have regard, by mentioning employee interests, s.279(4) CAMA appears to impose upon the director a duty to employees which s.279(9) clearly ousts them from enforcing. Furthermore, the mere mention of the matters to which the director may have regard encroaches upon his subjective judgment

regarding what is the best interests of the company at all times. S.172(1)(a-(e) CA is faulty for the same reason.

3. On the duty to act within powers

s.279(5) CAMA is replete with grammatical errors and set in vague terms. It does not adequately inform the director of the powers referred to. For example, are they powers under the Act or stated in his contract or provided in the articles? A novice director seeking to be informed here is unlikely to clearly comprehend the purport of the provision without the help of professional interpretation. In stark contrast, s.171 CA makes adequate and clear reference to the powers of the director alluded to.

4. On the duty to exercise independence

The provision in s.279(6) CAMA on this duty is clearly outdated in that it restricts the principle to voting situations and does not take cognizance of current practice whereby directors of companies may be required to bind themselves to act or vote in a particular way in the future in order to properly discharge the company's contractual obligations with third parties. Further, s.279(8) CAMA does not allow the articles to permit directors to act thus. This has the potential of making companies unreliable contracting partners. Case law from England has shown that the courts are amenable to such situations, given the exigencies of business practice, particularly with respect to agreements with creditors. S.173 CA commendably reflects this modern view.

5. On conflicts of duties and interests

S.280(1) CAMA on the duty above, is stated in general terms and neglects to clearly identify the well-known interests of the company often referred to, i.e. property, information and opportunity as identified in s.281 CAMA. Furthermore, it does not recognize the exception in situations of transactions or contracts with the company, which are already admitted by s.277 CAMA. S. 280(2) and (3) CAMA also use the vague and nebulous term "unnecessary benefit" which does not adequately describe to the director the kind of gain or profit which he must resist but even appears to allow his

subjective judgment on it. Further, subsections 280(5) and (6) respectively refer to "the duty not to misuse corporate information" and "the transaction", neither of which terms has been previously discussed earlier in the section, so that the use of the definite article "the" is misguided. Finally, with respect to a former director, S.280(5) CAMA seems to suggest that only corporate information is off limits to him, so that he is free to use corporate property and opportunity. On these points, s.175 CA appears to be comprehensive and clear, more so because it clearly informs the director of exceptions to the rule as well as situations which would not amount to breach.

6. On the prohibition of secret benefits

On this duty, the tenor of s.287(1) CAMA appears to restrict the application of the rule to the motive of inducement, i.e. cases where the director accepted the bribe, gift or commission in order to induce his company to deal with such a person. Thus, where the gift or commission is received by the director without any evidence of corrupt motive or where it is apparent that the director was actually unaffected, the rule under the section would not apply. It is submitted that this allows the director more room for dubious dealings. After all, most of such "gifts" are unlikely to be received with a "corrupt" motive, especially where it is considered customary. A director can also claim to be "unaffected" yet this should not allow him to unlawfully profit from his position. The same goes for the requirement that the gift be "unsolicited" if he is to be allowed to keep it. Again, the law does not hold a former director bound by the duty, so that a director may resign and then accept the "gift". These defects are not to be found in s.176 CA, where the law is clear, leaving no room for the director's subjective judgment as to instances in the matter of accepting benefits. The provision is also clear on what constitutes third party, admits the reasonability doctrine in determining liability and rightly expects the duty from a former director.

7. **on declaring interests in proposed or existing transactions**

S.277 CAMA only requires a declaration of the nature and not the extent of interest. This will not allow for a better informed decision on the matter. The section does not contemplate a situation whereby a further declaration be made when the director's interest changes or is discovered to have been inadequate in the first place. This canallow dubious directors to make inadequate declaration in order to claim later that they had declared what, at the time, was known to them S. 277 CAMA also seems to admit of no exceptions to the rule and would seem to require declaration of even matters which the director may not be aware of, or which is already known to the other directors. The fine of N100 is also ridiculously small, considering the value of the naira today. The duty is clearer under s. 177 CA which requires a declaration of both the nature and extent of interest, clearly allowing for a more informed decision on the matter. The law requires a further declaration to update information earlier given and clearly delineates instances where a declaration will not be unreasonably required. Neither law requires the matter to be considered by a 'disinterested' board, especially with respect to proposed transactions. Hence, the interested director, together with his cronies and any persons connected with him, can sit to decide that the company would still go ahead with the contract, in spite of the nature and extent of the directors' interests.

6.4 Recommendations

In view of the findings outlined above, the following recommendations are proffered:[2]

1. **On the duty of care and skill**

Considering the fact that society expects much more from the director today and also in view of the fact that directors today more often have several qualifications, the company should be entitled to expect more from the person who presents himself as skilful in a

[2] See Appendix B for a more comprehensive draft proposal of a statement of directors' duties.

particular field, even without a service contract with the company. Thus, even a non executive director, where he happens to be knowledgeable or skilful in a particular area, should be held to those standards as a default rule, even in the absence of a service contract. Therefore, s.282 CAMA should be amended to reflect the model in s.174 CA by which directors are held to an added subjective standard. This will encourage better appointments and prospective directors would pay more attention to their capabilities and responsibilities more seriously. In the long run, companies and investors will benefit from better corporate governance.

2. On the duty to act in the best interests of the company

Particularly for limited liability companies which are more prevalent—and therefore, in whose favour the default rule should be stated—the interests of the company cannot be distinguished from the interests of the members who stand to gain from it. Thus, s.279(3) CAMA should be amended to reflect this factual position in terms of s.172(1) CA, with a proviso with respect to companies limited by guarantee allowing the director to focus on achieving its stated objects as reflected in s.172(3) CA. S.279(4) should be completely abrogated as having no support under the law.

3. On the duty to act within powers

There is a need to amend s.279(5) CAMA to properly refer to the articles as the source of the powers referred to in order to better clarify to the director where he may acquaint himself with them. The style adopted in s.171 CA presents a simple and concise model and if adopted, will avoid the unnecessary verbosity and grammatical errors now contained in s.279(5) CAMA.

4. On the duty to exercise independence

S.279(6) CAMA must be amended to require independence in all judgments not only in voting situations. S.279(8) CAMA should also admit the modern exigency in business whereby directors may be required to fetter their discretion to vote in the interest of the company in order to fulfil obligations the company may have with third parties. At

least, the default rule should allow the articles to admit this as an exception to the general rule, as is the case with s.173 CA.

5. On conflicts of duties and interests

There is a need to comprehensively amend s.280 CAMA in order to better clarify the situations of conflict, exceptions to the rule and instances when a breach will not be said to have occurred. This will help the director more easily determine when he is likely to breach the duty. The model presented by s.175 CA should be adopted, while retaining s. 280(6) CAMA on the procedure for disclosure.

6. On the prohibition of secret benefits

S. 287 CAMA needs to be amended in order to leave no room for the director to manipulate situations and make gains at the company's expense. The gift or benefit need not be received with the motive of inducement and need not be unsolicited to be prohibited. Also, the duty should be required of a former director. An amendment is suggested, preferably in line with s.176 CA which is more comprehensive and couched in clearer terms.

7. On declaring interests in proposed or existing transactions

s.277 CAMA should be amended to require the declaration of both nature and extent of interest involved and also a further declaration when the need arises. Exceptions to the rule should be reasonably recognised and outlined, especially where the director is unaware of the transaction or where the situation cannot reasonably be regarded as likely to give rise to a conflict. S.177 CA is clear on these terms and should be adopted. The amendment should also require the consideration of the transaction by a disinterested board. With respect to fine, something within the range of N100,000 or more should be considered.

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APPENDIX A

Sections 170-180 of the UK Companies Act 2006

CHAPTER 2

GENERAL DUTIES OF DIRECTORS

Introductory

170 Scope and nature of general duties

(1) The general duties specified in sections 171 to 177 are owed by a director of a company to the company.

(2) A person who ceases to be a director continues to be subject—

(a) to the duty in section 175 (duty to avoid conflicts of interest) as regards the exploitation of any property, information or opportunity of which he became aware at a time when he was a director, and

(b) to the duty in section 176 (duty not to accept benefits from third parties) as regards things done or omitted by him before he ceased to be a director. To that extent those duties apply to a former director as to a director, subject to any necessary adaptations.

(3) The general duties are based on certain common law rules and equitable principles as they apply in relation to directors and have effect in place of those rules and principles as regards the duties owed to a company by a director.

(4) The general duties shall be interpreted and applied in the same way as common law rules or equitable principles, and regard shall be had to the corresponding common law rules and equitable principles in interpreting and applying the general duties.

(5) The general duties apply to shadow directors where, and to the extent that, the corresponding common law rules or equitable principles so apply.

171 Duty to act within powers

A director of a company must—

(a) act in accordance with the company's constitution, and

(b) only exercise powers for the purposes for which they are conferred.

172 Duty to promote the success of the company

(1) A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—

(a) the likely consequences of any decision in the long term,

(b) the interests of the company's employees,

(c) the need to foster the company's business relationships with suppliers, customers and others,

(d) the impact of the company's operations on the community and the environment,
(e) the desirability of the company maintaining a reputation for high standards of business conduct, and
(f) the need to act fairly as between members of the company.
(2) Where or to the extent that the purposes of the company consist of or include purposes other than the benefit of its members, subsection (1) has effect as if the reference to promoting the success of the company for the benefit of its members were to achieving those purposes.
(3) The duty imposed by this section has effect subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company.

173 Duty to exercise independent judgment
(1) A director of a company must exercise independent judgment.
(2) This duty is not infringed by his acting—
(a) in accordance with an agreement duly entered into by the company that restricts the future exercise of discretion by its directors, or
(b) in a way authorised by the company's constitution.

174 Duty to exercise reasonable care, skill and diligence
(1) A director of a company must exercise reasonable care, skill and diligence.
(2) This means the care, skill and diligence that would be exercised by a reasonably diligent person with—
(a) 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, and
(b) the general knowledge, skill and experience that the director has.

175 Duty to avoid conflicts of interest
(1) A director of a company must avoid a situation in which he has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company.
(2) This applies in particular to the exploitation of any property, information or opportunity (and it is immaterial whether the company could take advantage of the property, information or opportunity).
(3) This duty does not apply to a conflict of interest arising in relation to a transaction or arrangement with the company.
(4) This duty is not infringed—
(a) if the situation cannot reasonably be regarded as likely to give rise to a conflict of interest; or
(b) if the matter has been authorised by the directors.
(5) Authorisation may be given by the directors—

(a) where the company is a private company and nothing in the company's constitution invalidates such authorisation, by the matter being proposed to and authorised by the directors; or
(b) where the company is a public company and its constitution includes provision enabling the directors to authorise the matter, by the matter being proposed to and authorised by them in accordance with the constitution.
(6) The authorisation is effective only if—
(a) any requirement as to the quorum at the meeting at which the matter is considered is met without counting the director in question or any other interested director, and
(b) the matter was agreed to without their voting or would have been agreed to if their votes had not been counted.
(7) Any reference in this section to a conflict of interest includes a conflict of interest and duty and a conflict of duties.

176 Duty not to accept benefits from third parties
(1) A director of a company must not accept a benefit from a third party conferred by reason of—
(a) his being a director, or
(b) his doing (or not doing) anything as director.
(2) A "third party" means a person other than the company, an associated body corporate or a person acting on behalf of the company or an associated body corporate.
(3) Benefits received by a director from a person by whom his services (as a director or otherwise) are provided to the company are not regarded as conferred by a third party.
(4) This duty is not infringed if the acceptance of the benefit cannot reasonably be regarded as likely to give rise to a conflict of interest.
(5) Any reference in this section to a conflict of interest includes a conflict of interest and duty and a conflict of duties.

177 Duty to declare interest in proposed transaction or arrangement
(1) If a director of a company is in any way, directly or indirectly, interested in a proposed transaction or arrangement with the company, he must declare the nature and extent of that interest to the other directors.
(2) The declaration may (but need not) be made—
(a) at a meeting of the directors, or
(b) by notice to the directors in accordance with—
(i) section 184 (notice in writing), or
(ii) section 185 (general notice).
(3) If a declaration of interest under this section proves to be, or becomes, inaccurate or incomplete, a further declaration must be made.
(4) Any declaration required by this section must be made before the company enters into the transaction or arrangement.

(5) This section does not require a declaration of an interest of which the director is not aware or where the director is not aware of the transaction or arrangement in question. For this purpose a director is treated as being aware of matters of which he ought reasonably to be aware.
(6) A director need not declare an interest—
(a) if it cannot reasonably be regarded as likely to give rise to a conflict of interest;
(b) if, or to the extent that, the other directors are already aware of it (and for this purpose the other directors are treated as aware of anything of which they ought reasonably to be aware); or
(c) if, or to the extent that, it concerns terms of his service contract that have been or are to be considered—
(i) by a meeting of the directors, or
(ii) by a committee of the directors appointed for the purpose under the company's constitution.

Supplementary provisions

178 Civil consequences of breach of general duties

(1) The consequences of breach (or threatened breach) of sections 171 to 177 are the same as would apply if the corresponding common law rule or equitable principle applied.
(2) The duties in those sections (with the exception of section 174 (duty to exercise reasonable care, skill and diligence)) are, accordingly, enforceable in the same way as any other fiduciary duty owed to a company by its directors.

179 Cases within more than one of the general duties

Except as otherwise provided, more than one of the general duties may apply in any given case.

180 Consent, approval or authorisation by members

(1) In a case where—
(a) section 175 (duty to avoid conflicts of interest) is complied with by authorisation by the directors, or
(b) section 177 (duty to declare interest in proposed transaction or arrangement) is complied with,
the transaction or arrangement is not liable to be set aside by virtue of any common law rule or equitable principle requiring the consent or approval of the members of the company.
This is without prejudice to any enactment, or provision of the company's constitution, requiring such consent or approval.
(2) The application of the general duties is not affected by the fact that the case also falls within Chapter 4 (transactions requiring approval of members), except that where that Chapter applies and—
(a) approval is given under that Chapter, or

(b) the matter is one as to which it is provided that approval is not needed, it is not necessary also to comply with section 175 (duty to avoid conflicts of interest) or section 176 (duty not to accept benefits from third parties).
(3) Compliance with the general duties does not remove the need for approval under any applicable provision of Chapter 4 (transactions requiring approval of members).
(4) The general duties—
(a) have effect subject to any rule of law enabling the company to give authority, specifically or generally, for anything to be done (or omitted) by the directors, or any of them, that would otherwise be a breach of duty, and
(b) where the company's articles contain provisions for dealing with conflicts of interest, are not infringed by anything done (or omitted) by the directors, or any of them, in accordance with those provisions.
(5) Otherwise, the general duties have effect (except as otherwise provided or the context otherwise requires) notwithstanding any enactment or rule of law.

APPENDIX B

Comprehensive Draft Proposal of a Statement of Directors' Duties for the Amendment of the Companies and Allied Matters Act 1990

Based on the findings reached in this work, it is hereby recommended that:

1. The various provisions on fiduciary duties and duties of care and skill within the CAMA be arranged in the same part of the Act and seriatim;
2. Each duty be specified and identified by an explanatory heading in a particular section as per the CA;
3. The principles codified in ss.279(1), (2) and (9) and 280(5) CAMA, be restated in terms of their equivalent in the CA as an introductory section to the directors' duties thus:
    i) Subject to the provisions of this Act, the duties specified in sections – to – are owed by a director of a company to the company and are therefore enforceable against the director by the company.
    ii) Subject to any necessary adaptations, a former director continues to be subject to the duty to avoid conflicts of interest and the duty not to accept benefits from third parties.
    iii) The general duties apply to a shadow director to the extent of any directions or instructions he/she gives.
    iv) A director of a company stands as a fiduciary to that company and must observe the utmost good faith towards the company in any action on its behalf.
4. The principle in s.279(5) CAMA be reviewed per s.171 CA thus:
    A director of a company must—
    i) act in accordance with the company's constitution, and

ii) only exercise powers for the purposes for which they are conferred.

Consequently, a preliminary provision introductory to the CAMA should reflect that the articles together with any special resolutions and agreements of members constitute the company's constitution.

5. The principle in s.279(3) and (4) CAMA be reviewed thus:
   "A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard to matters most likely to promote the success of the company.
   Where the company is limited by guarantee, subsection (1) has effect as if the reference to promoting the success of the company for the benefit of its members were to achieving its objects.
   The duty imposed by this section is subject to the provisions of this Act relating to the interest of creditors as well as any rule of law or Act requiring directors to have regard to any particular matter."
6. The principle in s.279(6) CAMA be reviewed in accordance with s.173 CA
7. The principles in ss.279(7) and 282 CAMA be reviewed and partly restated as per s.174 CA in addition to retaining s.279(7) CAMA.
8. The principles in s.280(1), (2), (3), (4) and (6) CAMA be restated in terms of s.175 CA with the following alterations:
   i) Omitting "by the directors" in 175(4)(b)
   ii) Substituting 175(5) with:
   Authorisation, in the case of—
   a private company, may be given by the directors, where the company's articles includes provisions enabling the directors to authorise the matter;
   a public company, must be given by the members.
   iii) Inserting the following words in the beginning of s.175(6):
   In the case of authorisation by the directors in a private company,…
   iv) Adding a rider at the end of 175(6)(b) thus:
   the company's articles maymakefurther provisions for dealing with conflicts of interest.
9. The principle in s.287 CAMA be reviewed and stated in terms of s.176 CA with the following alterations:
   i) Omitting s.176(3) and
   ii) Inserting an additional subsection as follows:
   where the benefit offered is disclosed to, and approved by the general meeting, the director may take it.
10. The principle in s.277 CAMA be reviewed and restated in terms of s.177 CA with the following alterations:
    i) Removing "a proposed transaction or arrangement" in s.177(1) CA and replacing with "any proposed contract or contract that has been entered into"
    ii) Removing s.177(4) and Inserting a rider to s.177(2): "any declaration required to be made by this section must be made as soon as is

reasonably practicable, in the case of an existing contract, and before the company enters into the contract, in the case of a proposed contract."

iii) Inserting a subsection: "where disclosure is made regarding a proposed transaction, the matter must be referred to the general meeting for approval."

iv) Inserting a subsection stating: "a company director who fails to comply with the provisions of this section regarding disclosure, commits an offence and is liable to a fine of N100,000.00"

Inserting a further subsection stating: "nothing in this section shall prejudice the rule as to substantial property transactions involving directors."