

LOCAL LEGAL EXPERTS CLARIFY POINTS OF CONCERN IN NEW COMPANIES ACT

The Companies Act 2006, which received the Royal Assent on 8 November 2006, represents the largest overhaul of company law since 1985 and replaces almost entirely the Companies Acts of 1985 and 1989. At 1,300 sections and 16 schedules, the Act is believed to be the largest Act of Parliament on the statute books.

The Act will provide a simpler regulatory regime for private limited companies and to accompany this simplification, there is to be, for the first time in the UK, a statutory code of director's duties. These are contained in 7 "general duties" as follows:

- 1 A duty to act within powers
- 2 A duty to promote the success of the company
- 3 A duty to exercise independent judgment
- 4 A duty to exercise reasonable skill, care and diligence
- 5 A duty to avoid conflicts of interest
- 6 A duty not to accept benefits from third parties
- 7 A duty to declare interest in proposed transactions or arrangement.

These duties do not replace the existing case law on director's duties, much of which will continue to apply in the interpretation and application of the new statutory code. The key elements established in case law of:- obedience to lawful instructions; the use of appropriate care and skill; the exercise of appropriate diligence; and the requirement to act in good faith will still apply.

However, the statutory code introduces two new provisions. The duty to act in good faith, in the best interests of the company, is expanded by imposing upon the directors an obligation to have regard (amongst other matters) to a statutory list of 6 specific concerns which include:- the interests of employees; and the impact of the company's operations on the community and the environment.

The common law duty to act in good faith in the avoidance of conflict of interest is also amended to allow directors to be personally interested in transactions or arrangements made with their company, provided that such interest is disclosed to the Board and the transaction or arrangement is authorised by the Board at a meeting, without counting the vote of the director involved. The effect of this new concept of authorisation by the Board is that transactions between a director and his or her company may now be permitted which would previously have fallen foul of the common law duty to act in good faith and to avoid conflicts of interest.

The consequences of a breach of the new statutory code are the same as would apply if the corresponding common law or equitable principle applied to the breach. The duties in the statutory code are, accordingly, enforceable in the same way as any other fiduciary duty owed to a company by its directors. However, in order to give teeth to the requirement for a director to declare an interest in any transaction or arrangement with his or her company, the Act introduces a criminal offence of failing to comply with the disclosure requirements.

Most of the changes introduced by the 2006 Act are not due to come in to force until October 2008 but the Act should be welcomed by the directors of private limited companies as a simpler and more “user friendly” regulatory regime. However, directors need to be careful if they are not to be caught out by the detail. Expert legal advice should be sought by all directors regarding the application of the new rules, before they become effective.

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