Notes:

[1] It is important to be aware of the differences between executive and non-executive directors (see 'Balance of executive and non-executive directors', p 264); appointed, *de facto* and shadow directors ('Directors' duties are owed by *de jure* and *de facto* directors', pp 311ff); alternate directors and nominee directors. These different categories are not mutually exclusive.

[2] CA 2006 Model Articles for Private Companies art 17, provides for appointment by *either* the general meeting or the board of directors. There is the same provision for public companies (Model Articles art 20), but if the appointment is made by the directors it is subject to confirmation by the members (art 21).

[3] *Worcester Corsetry Ltd v Witting* [1936] Ch 640.

[4] In *Theseus Exploration NL v Mining and Associated Industries Ltd* [1973] Qd R 81, the court issued an interim injunction to prevent members of the company electing certain persons as directors, because there was sufficient evidence that those persons intended to use the company's assets solely for the benefit of the majority member.

[5] Recall that the functions of a managing director are not set by law: *Harold Holdsworth & Co (Wakefield) Ltd v Caddies* [1955] 1 WLR 352, HL.

[6] See the discussion at 'Members' personal rights', pp 250ff.

[7] [1946] AC 459.

[8] The House of Lords affirmed the decision of the Court of Appeal on grounds that did not raise this question.

[9] Eg for public companies, see Model Articles art 21; there is no equivalent in the Model Articles for private companies.

[10] The predecessor section, CA 1985 s 303, also indicated that the right was 'notwithstanding anything in the articles', but, since the Act overrides the articles, this was seen as unnecessary.

[11] Although note the practical impediment of having to give special notice, and hold a meeting: see 'Removal of directors', pp 284ff.

[12] The removal of a director may sometimes justify the making of a winding-up order on the 'just and equitable' ground, at least in a small company (see 'Compulsory winding up on the "just and equitable" ground', pp 795ff), or, alternatively, amount to 'unfairly prejudicial' conduct within CA 2006 s 994 (see 'Unfairly prejudicial conduct of the company's affairs', pp 681ff).

[13] CA 2006 s 168 does not deprive the director of any compensation or damages payable in respect of termination of the appointment as director or of any appointment terminating with that as director (s 168(5)(a)).

[14] Although note that the director is subject to the usual common law duty to mitigate his or her damages by seeking substitute employment, ie the director is not automatically entitled to be 'paid out' to the end of the contractual term.

[15] (1864) 5 B & S 840 at 852.

[16] [1914] 2 KB 770. [See the Note following.]

[17] In *Dafen Tinplate Co Ltd v Llanelly Steel Co (1907) Ltd* **[4.25]**.

[18] Or may direct the Official Receiver to make the application, if it comes under CDDA 1986 s 6.

[19] See A Walters, 'Directors' Duties: Impact of the CDDA?' (2000) 21 *Company Lawyer* 110.

[20] Especially when the possible liability of directors for wrongful trading (*Re Produce Marketing Consortium Ltd (No 2)* **[16.16]**) is also taken into account.

[21] This difficulty was initially overcome by judicial ingenuity: under what was known as the '*Carecraft*' procedure (named after *Re Carecraft Construction Co Ltd* [1993] 4 All ER 499), if a director was willing to concede that a finding of unfitness was appropriate, and also agree that a period of disqualification within a certain range (say, four to six years) was merited, the court could proceed on the basis of an agreed statement of facts and dispose of the case without a full hearing. This procedure remains available, but in practice it has been overtaken by the improved statutory provisions.

[22] www.judiciary.gov.uk/Resources/JCO/Documents/Judgments/farepak-judges-statement.pdf.

[23] [1988] Ch 477 at 486.

[24] [1990] BCLC 668 at 671.

[25] [1987] BCLC 601.

[26] Cheque kiting can take a number of different forms. At the heart of the process is the utilisation by the kiter of the period taken by the bank to clear a cheque so as to obtain a fictional increase in the balance of the payee's account before the cheque is cleared and its amount is deducted from the payer's account. It can therefore be used as a means to generate fictitious funds which may then be misappropriated or used to cover short-term cash-flow problems, or simply to create the false impression of a healthier bank balance or cash-flow than would otherwise be the case.

7. Directors' Duties

Chapter: **(p. 309)** 7. Directors' Duties
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General issues

Directors normally have exclusive power to manage the business of the company. The advantage of a board of directors is both concentrated expertise, relative independence from the company's various stakeholders (eg members or shareholders, and executive management) and the efficiency of centralised decision-making. The disadvantage, however, is that the directors may manage the company in their own interests rather than in the interests of those they are supposed to serve. There are several ways of addressing this risk.

One option is to give more power to the members. Clearly it would not help to have the members make all the company's decisions. However, in earlier chapters we saw that certain crucial decisions are reserved to the members and that they have the power to remove the directors by ordinary resolution, with all the benefits that this implies by way of implicit or explicit threat to underperforming directors. Another option is to insist on certain governance arrangements within the board of directors and certain procedures in the decision-making process itself. Again, in Chapter 5 we saw that the UK Corporate Governance Code for public listed companies sets out rules of best practice for the composition of the board and its various subcommittees. In addition, adequate disclosure to those likely to be most affected by the activities of the directors is always helpful. That, too, is required by the Companies Act 2006 (CA 2006) Pt 15 (requirements for accounts and directors' reports, including the forward-looking '*business review*')[1] and, for larger companies, Pt 16 (requirement for audited accounts).

All of these regimes are directed at creating incentives (or threats) to improve directors' performance. But the third option for dealing with the various agency problems arising from centralised decision-making is the one most familiar to lawyers: legal duties are imposed on directors which set limits within which they must exercise their powers. These legal duties are the subject of this chapter.

Historically, these duties were developed by the courts of equity, largely by analogy with the rules applying to trustees (the roles have fundamental similarities, but also certain important differences[2]). One of the most significant changes introduced by CA 2006 Pt 10 is to codify these common law and equitable duties applying to directors.

(p. 310) Codification was recommended by the Law Commissions,[3] and the Company Law Review (CLR) published a draft code in its Final Report,[4] along with extensive commentary.[5] The primary reason for recommending codification was to make the relevant rules clear and accessible—for both directors and those affected by their decisions. CA 2006 s 170 sets out the scope and nature of the codified general duties, and these then follow in successive sections:

(i) duty to act within powers (s 171): see 'Duty to act within powers: CA 2006 s 171', pp 331ff;
(ii) duty to promote the success of the company (s 172): see 'Duty to promote the success of the company: CA 2006 s 172', pp 339ff;
(iii) duty to exercise independent judgement (s 173): see 'Duty to exercise independent judgement: CA 2006 s 173', pp 350ff;
(iv) duty to exercise reasonable care, skill and diligence (s 174): see 'Duty to exercise reasonable care, skill and diligence: CA 2006 s 174', pp 353ff;
(v) duty to avoid conflicts of interest (s 175): see 'Duty to avoid conflicts of interest: CA 2006 s 175', pp 361ff;
(vi) duty not to accept benefits from third parties (s 176): see 'Duty not to accept benefits from third parties: CA 2006 s 176', pp 408ff;
(vii) duty to declare an interest in a proposed or existing transaction or arrangement (ss 177 and 182): see

'Duty to declare an interest in a proposed or existing transaction or arrangement: CA 2006 ss 177 and 182', pp 409ff.

This codification supersedes the older case law. But those cases will remain relevant to the interpretation of the new statutory provisions, since the codified duties are generally formulated in a way that quite faithfully reflects the older case law. Indeed, the rules set out in the Act are deliberately expressed at a sufficiently high level of generality so as to be capable of judicial development within their terms, and the Act itself provides a novel mechanism for applying and interpreting a statute: it *requires* the courts to have regard to the existing interpretation and continuing development of the common law rules and equitable principles on which the statutory statement is based when interpreting and applying the statutory statement (s 170(3) and (4)). This approach is not normally allowed in interpreting the words of a statute.

Commentators have noted that all the rules are now formulated as 'duties', although it is not clear what, if any, practical significance attaches to this (although clearly Vinelott J's distinction in *Movitex v Bulfield*[6] between a 'duty' and a 'disability' will no longer be recognised).

The remedies for breach have not been codified. The common law and equitable rules are simply imported into the Act (s 178): see 'General issues', pp 413ff. But the protective rules that allow certain activities, which might otherwise constitute breaches to be authorised (before the event) or ratified (afterwards) have been codified. Additionally, a new ban on implicated directors voting as shareholders in ratifying resolutions (ss 180 and 239) has been included: see 'Ratification of acts of directors: CA 2006 s 239', pp 437ff. This means that many older authorities will be relegated to oblivion,[7] and others reappraised, particularly those involving small companies where the quest for 'independent' shareholders may well be a meaningless exercise.

Finally, these duties are mandatory. CA 2006 s 232(1) provides: 'Any provision that purports to exempt a director of a company (to any extent) from any liability that would otherwise attach **(p. 311)** to him in connection with any negligence, default, breach of duty or breach of trust in relation to the company is void.' It is irrelevant whether the provision is contained in the articles or in a separate contract. Section 232 merits reading in full for the few qualifications it does permit.

Additional rules

In working through this chapter, do not forget that directors are subject to various other rules and regulations. CA 2006 itself imposes substantial disclosure obligations, noted earlier, and there are various rules that apply when directors seek funding for the company (see Chapters 9, 11 and 12), or make use of the company's capital and profits (see Chapter 10). Breach of these rules may attract criminal sanctions, as well as civil ones.

The Insolvency Act 1986 (IA 1986) also empowers the court to review directors' conduct in the period leading up to insolvency, and to penalise directors who have failed to operate according to the statutory standards (see Chapter 16).

In addition, if a company goes into insolvent liquidation or administration, or an administrative receiver is appointed, a director whose conduct makes him 'unfit to be concerned in the management of a company' may have a disqualification order made against him (see 'Directors' disqualification', pp 294ff).

For the purpose of applying these various sanctions, the courts are free (and, in some cases, expressly directed) to assess the conduct of a director by objective standards. The context of insolvency also removes many (but not all) of the problems associated with proving causation and quantifying loss.

As a result of these differences, the developing law on directors' duties has in the past few decades been driven to a much greater extent by rulings under the statutory provisions just mentioned (including, to some extent, by proceedings under the Companies Act 1985 (CA 1985) s 459 (now CA 2006 s 994, relief for 'unfairly prejudicial conduct': see 'Unfairly prejudicial conduct of the company's affairs', pp 681ff)) than by traditional case law dealing with the general duties of directors (now themselves codified).

For example, the judgment in *Re Barings plc (No 5)* **[6.12]** (a disqualification case) contains leading statements on the duty of senior directors to ensure that proper management systems within the company are maintained. It is

doubtful whether any claim against these directors would have succeeded (or even been brought) at common law (or under the new codified provisions in CA 2006), because of the difficulty in establishing that the directors' failure to discharge this duty was the cause in law of the company's loss.

Finally, in all this discussion of the duties directors owe their companies, do not forget that directors may, in some circumstances, be found personally liable *to* third parties who have dealt with the company. Recall *Williams v Natural Life Health Foods Ltd* **[3.22]** (where the claim for negligent misstatement was unsuccessful) and *Standard Chartered Bank v Pakistan National Shipping Corpn (No 2)* **[3.23]** (where the claim in deceit was successful).

Directors' duties are owed by *de jure* and *de facto* directors

Section 250 defines 'director' as including 'any person occupying the position of director, by whatever name called'. This means these general duties apply equally to *de facto* directors.[8] And notice **(p. 312)** s 170(2), which applies *some* of the statutory duties to former directors: see 'Statutory changes to the equitable rules', p 370. The position with *shadow directors* (see the following section) is less clear. Section 170(5) says shadow directors are subject to the duties to the same extent that, before the Act, they were subject to the corresponding common law rules and equitable principles. The difficult decision is thus left to the courts. For example, the mere fact that a person is a shadow director, and exercises indirect influence, is, it seems, not enough to impose fiduciary duties: the facts must go further and suggest that there is a fiduciary relationship (*Ultraframe (UK) Ltd v Fielding* **[7.44]**). The merits of this restrained approach to shadow directors deserve further consideration.[9]

'Shadow directors': s 251

A 'shadow director' is defined as 'a person in accordance with whose directions or instructions the directors of a company are accustomed to act'. The court in *Ultraframe (UK) Ltd v Fielding* **[7.44]** interpreted this as meaning that at least a consistent majority of the directors must be accustomed to act in that way. If only a minority of the company's directors are accustomed so to act, it is not enough to make the person a shadow director (*Lord v Sinai Securities Ltd* [2004] EWHC 1764 (Ch)).

Section 251(2), however, excludes a professional person on whose advice the directors act. The definition of a 'shadow director' appears to preclude persons from being both a shadow director and a *de jure* director (*Re Hydrodam (Corby) Ltd* [1994] 2 BCLC 180), but this is not explicit in the section.

Distinguishing de facto and shadow directors.

[7.01] Re Hydrodam (Corby) Ltd [1994] 2 BCLC 180

> MILLETT J: I would interpose at this point by observing that in my judgment an allegation that a defendant acted as de facto or shadow director, without distinguishing between the two, is embarrassing. It suggests —and counsel's submissions to me support the inference—that the liquidator takes the view that de facto or shadow directors are very similar, that their roles overlap, and that it may not be possible to determine in any given case whether a particular person was a de facto or a shadow director. I do not accept that at all. The terms do not overlap. They are alternatives, and in most and perhaps all cases are mutually exclusive.
>
> A de facto director is a person who assumes to act as a director. He is held out as a director by the company, and claims and purports to be a director, although never actually or validly appointed as such. To establish that a person was a de facto director of a company it is necessary to plead and prove that he undertook functions in relation to the company which could properly be discharged only by a director. It is not sufficient to show that he was concerned in the management of the company's affairs or undertook tasks in relation to its business which can properly be performed by a manager below board level. …
>
> A shadow director, by contrast, does not claim or purport to act as a director. On the contrary, he claims not to be a director. He lurks in the shadows, sheltering behind others who, he claims, are the only directors of the company to the exclusion of himself. He is not held out as a director by the company. To establish that a defendant is a shadow director of a company it is necessary to allege and prove: (1) who

> are the directors of the company, whether de facto or de jure; (2) that the defendant directed those directors how to act in relation to the company or that he was one of the persons who did so; (3) that those directors acted in accordance with such directions; and (4) that they were accustomed so to act. What is needed is, first, a board of directors claiming and **(p. 313)** purporting to act as such; and, secondly, a pattern of behaviour in which the board did not exercise any discretion or judgment of its own, but acted in accordance with the directions of others.

➤ Notes

1. In appropriate cases, a holding company (and possibly also its directors), a consultant called into assist in a corporate rescue and a company's bank could be held to be 'shadow directors' **.** But for this to be the case, the whole board has to act in accordance with the shadow director's instructions or directions.

2. In *Ultraframe (UK) Ltd v Fielding* **[7.44]** it was held that the fact that the directors of a company are obliged to conduct it in accordance with requirements laid down by a major lender or customer for the protection of that person's interests does not necessarily make that person a shadow director.

3. The leading judicial analysis of the concept of shadow director is to be found in the judgment of Morritt LJ in *Secretary of State for Trade and Industry v Deverell* [2001] Ch 300, CA. In particular, Morritt LJ stressed that its interpretation may depend on the statutory context (eg a stricter construction may be more appropriate in a criminal or quasi-criminal provision); that the purpose of the legislation is to identify those with 'real influence' in the corporate affairs of the company, or part of them; that advice (other than professional advice) is capable of coming within the phrase 'directions or instructions'; and that it is not necessary that the board should be reduced to a subservient role or surrender its discretion.

4. In *Re Hydrodam*, Millett J added some further observations as to what is required before the director of a corporate director can be classified as *de facto* director of the company:

> Attendance of board meetings and voting, with others, may in certain limited circumstances expose a director to personal liability to the company of which he is a director or its creditors. But it does not, without more, constitute him a director of any company of which his company is a director.

As to what that 'something more' may entail, and the difficulties which can arise in applying the test, see the next case.

Whether the director of a corporate director of company A is himself a de facto director of company A depends upon whether he does more than merely discharge his duties as director of the corporate director.

[7.02] Revenue and Customs Commissioners v Holland [2010] UKSC 51, [2010] 1 WLR 2793 (Supreme Court)

A complex corporate structure was created to minimise the tax liabilities of contractors. This involved the setting up of 42 subsidiary companies within a corporate structure. The scheme failed, with the result that all 42 companies went into insolvency owing substantial unpaid tax which, in the circumstances, would not be recouped from the companies themselves. Each company had only one under-capitalised corporate director,[10] so an action against the companies' defaulting directors would not enhance recoveries. HMRC therefore brought proceedings against Mr Holland. He was the *de jure* director of the corporate director of each of the 42 insolvent companies, and HMRC alleged he was also the *de facto* director of each of the 42 companies, so was liable as a defaulting director for his role in contributing to the losses **(p. 314)** sustained by those companies. By a narrow majority (LORDS HOPE, COLLINS AND SAVILLE, with LORDS WALKER and CLARKE dissenting), the Supreme Court held that Mr Holland was only a *de jure* director of the corporate director, and not also a *de facto* director of the 42

companies.

LORD HOPE:

36 … Recalling that the essence of Millett J's reasoning in *Hydrodam* was that membership of the board of a corporate director will not, without more, make such member a shadow or de facto director of any company, he [Rimer LJ in the Court of Appeal's decision in *Holland*] said that he did not find anything in that judgment to suggest that the 'requisite more' would be satisfied merely by the active participation of the board member in the making of board decisions by the corporate director in relation to the actions of the subject company: para 66.

…

39 How is this to be done? It is plain from the authorities that the circumstances vary widely from case to case. Jacob J declined to formulate a single decisive test in*Secretary of State for Trade and Industry v Tjolle* [1998] 1 BCLC 333, as he saw the question very much as one of fact and degree. He was commended by Robert Walker LJ in *Re Kaytech International plc* [1999] 2 BCLC 351, 423 for not doing so, and I respectfully agree that there is much force in Jacob J's observation. All one can say, as a generality, is that all the relevant factors must be taken into account. But it is possible to obtain some guidance by looking at the purpose of the section. As Millett J said in *Re Hydrodam (Corby) Ltd* **[7.01]**, the liability is imposed on those who were in a position to prevent damage to creditors by taking proper steps to protect their interests. As he put it, those who assume to act as directors and who thereby exercise the powers and discharge the functions of a director, whether validly appointed or not, must accept the responsibilities of the office. So one must look at what the person actually did to see whether he assumed those responsibilities in relation to the subject company.

40 The problem that is presented by this case, however, is that Mr Holland was doing no more than discharging his duties as the director of the corporate director of the composite companies. Everything that he did was done under that umbrella. Mr Green QC for HMRC was unable to point to anything that he did which could not be said to have been done by him in his capacity as a director of the corporate director. When asked what it was that lay outside his performance of that role, he said that it was simply the quality of his acts. He did everything. He was the decision maker, and he was the person who gave effect to those decisions. In *Hydrodam***[7.01]** at p 184 Millett J rejected the proposition that, where a body corporate is a director of a company, whether it be de jure, de facto or shadow director, its own directors must ipso facto be shadow directors of the subject company. He said that attendance at board meetings and voting with others did not, without more, constitute him a director of any company of which his company is a director. That would not be a fair description of what Mr Holland did in this case. But in a later paragraph on p 184 Millett J said this:

> 'It is possible (although it is not so alleged) that the directors of Eagle Trust as a collective body gave directions to the directors of the company and that the directors of the company were accustomed to act in accordance with such directions. But if they did give such directions as directors of Eagle Trust, acting as the board of Eagle Trust, they did so as agents for Eagle Trust (or more accurately as the appropriate organ of Eagle Trust) and the result is to constitute Eagle Trust, but not themselves, shadow directors of the company.'

This passage indicates that the 'without more' requirement that Millett J had in mind would not be satisfied by evidence that the individual director of the body corporate was actually giving instructions in that capacity to the subject company and the subject company was accustomed to act in accordance with those directions. That would not be enough to prove that the individual director assumed a role in the management of the subject company which imposed responsibility on him for misuse of the subject company's assets.
…

(p. 315) 42 This was, I think, the point that Mr Knox was seeking to make when he referred to the speeches in *Salomon v A Salomon & Co Ltd* **[2.01]**. As Lord Davey said at p 54, the intention of the legislature must be collected from the language of its enactments. One can properly say, as Lord Macnaghten did about the company and its subscribers at p 51, that a company is at law a different person from its directors and that it is the intention of the enactment that this distinction should be recognised. I do not think that one can overcome this distinction by pointing, as Mr Green seeks to do, simply to the quality of the acts done by the director and asking whether he was the guiding spirit of the subject company or had a real influence over its affairs. As a test, that would create far too much uncertainty. Those who act as directors of a corporate director are entitled to know what it is that they can and cannot do when they are procuring acts by the corporate director. That is as true of a case such as this, where the affairs of the corporate director are effectively in the hands of one individual, as it is where there is a board comprised of several directors who always act collectively. As Lord Collins says (see paras 53 and 95, below), the question is one of law and it is a question of principle. I think that the guiding principle can be expressed in this way, unless and until Parliament provides otherwise. So long as the relevant acts are done by the individual entirely within the ambit of the discharge of his duties and responsibilities as a director of the corporate director, it is to that capacity that his acts must be attributed.

43 It is, of course, right to bear in mind the interests of the creditors. Their protection lies in the remedies that are available for breach of the fiduciary duty that rests on the shoulder of every director. But the essential point, which Millett J was at pains to stress in *Hydrodam*, is that for a creditor of the subject company to obtain those remedies the individual must be shown to have been a director, not just of the corporate director but of the subject company too. I agree with Rimer LJ that, on the facts accepted by the deputy judge, it has not been shown that Mr Holland was acting as de facto director of the composite companies so as to make him responsible for the misuse of their assets.

LORD WALKER (dissenting):

101 I am unable to agree with the reasoning and conclusions of the majority on the first issue in this appeal. The court's decision will, I fear, make it easier for risk-averse individuals to use artificial corporate structures in order to insulate themselves against responsibility to an insolvent company's unsecured creditors. …

114 Mr Holland was … the founder and guiding spirit of the whole Paycheck empire. With the concurrence of his wife (whose responsibilities were no more than secretarial) he was the only active director of both Paycheck Directors and Paycheck Secretarial; he was the original holder of all the A shares which carried voting control of the composite companies, and he was the only active director of the corporate trustee which held the A shares under settlements which he had created. He took the decision (after receiving the advice of leading counsel at the consultation on 18 August 2004) that composite companies should continue trading, and should continue to pay dividends without reserving for higher rate corporation tax.

115 If those facts did not amount to the 'something more' referred to in the authorities, it is hard to imagine circumstances that would do so. The repeated assertion that everything that Mr Holland did was done in his capacity as a director of Paycheck Directors, and was within his authority as a director of that company, is no doubt not 'pure sham' but it is, in my view, the most arid formalism. In my view Mr Holland was acting both as a de jure director of Paycheck Directors and as a de facto director of the composite companies. A de facto director is not formally invested with office, but if what he actually does amounts to taking all important decisions affecting the relevant company, and seeing that they are carried out, he is acting as a director of that company. It makes no difference that he is also acting as the only active de jure director of a corporate director of the company. …

117 Mr Green, for HMRC, relied strongly on the decision of the House of Lords in *Standard Chartered Bank v Pakistan National Shipping Corpn (Nos 2 and 4)* **[3.23]**. In that case Mr Mehra had made fraudulent misrepresentations on behalf of a company called Oakprime, of which he was a director. The Court of Appeal accepted the argument that he was not personally liable for deceit **(p. 316)** because he had been acting solely on behalf of Oakprime. The House of Lords trenchantly exposed the fallacy of this reasoning. …

118 … I will limit quotation to para 41 of Lord Rodger's opinion:

> 'The Court of Appeal sought support for their view that Mr Mehra should not be held personally liable in the speech of Lord Steyn in *Williams v Natural Life Health Foods Ltd* **[3.22]** … In truth it provides no such support. The issue in that case related to the personal liability of a director for a misleading projection [requiring an assumption of responsibility under the *Hedley Byrne* test] … There is no such requirement in the case of deceit. Liability for deceit is so self-evident that we do not consider it as resulting from a breach of duty (Tony Weir, *Tort Law* (2002), p 30). Mr Mehra set out by his fraudulent acts to make Standard Chartered pay under the letter of credit. He succeeded. He is accordingly personally liable for the loss which he thereby caused them.'

119 Mr Knox, for Mr Holland, summarily dismissed this case as irrelevant on the ground that it was a claim in deceit. So it was, and there has never been any pleading or finding of dishonesty against Mr Holland. Nevertheless there is to my mind a significant parallel between liability for deceit (which is in Lord Rodger's words 'so self-evident that we do not consider it as resulting from a breach of duty') and the unqualified statutory prohibition in section 263 of the Companies Act 1985 [CA 2006 s 830(1)] on payment of a dividend otherwise than out of available profits. Contravention of this prohibition is a statutory wrong giving rise to strict liability, and anyone who is in a position to contravene it is likely to be in a fiduciary position: see further below. Mr Holland was the human cause of (and apart from his wife's secretarial assistance, the only human being who took any part in) the payment of unlawful dividends. They were, as Rimer LJ said [in the Court of Appeal, see later], para 112, payments which should never have been made. Mr Holland is liable for the payments because he deliberately made them. His liability has nothing to do with limited liability of shareholders, or with *Salomon v A Salomon & Co Ltd* **[2.01]**. …

121 I agree with Lord Collins JSC that section 212 is procedural in nature, and that for liability to arise under the section, a breach of some identifiable duty must be established. I also agree that assumption of responsibility is the appropriate test, so long as that expression is understood as focusing on what the individual in question did, rather than what he was called: see the authorities mentioned in para 108 above. In this case the assumption of responsibility equates with the fiduciary duty that a company director owes to his company not to make an unauthorised distribution of capital. But in the circumstances of this case I think that there would be some element of putting the cart before the horse in looking for a fiduciary duty before looking at what Mr Holland did, because it is what he did that demonstrates that he was undertaking responsibility and exposing himself to a claim for breach of fiduciary duty. [He also referred to Lord Collins' 'monumental' first instance judgment in *Primlake Ltd v Matthews Associates* [2007] 1 BCLC 666, especially [311], in support.]

123 Lord Saville of Newdigate's brief judgment overlooks the important difference between a multiplicity of human directors participating in the collective governance of a single corporate director (as is common and as was the case, indirectly, in *In re Hydrodam* **[7.01]**), and a single individual director who is the guiding mind of a single corporate director, as Mr Holland was in this case.

➢ Questions

1. There are powerful arguments on both sides in this case. The case would never have arisen if it were not possible to have single corporate directors, and single (human) directors of corporate directors. Given CA 2006 s 155(1), which prevents single corporate directors, but not single human directors, are the arguments here now purely academic?

(p. 317) 2. The majority was concerned not to ride roughshod over the separate entity doctrine; the minority was concerned to impose appropriate liability (as the CA 2006 requires) on individuals who assume the role of *de facto* directors. Which analysis is more persuasive? Does the difference between the majority and the

minority turn on a matter of legal principle (per Lord Collins at [53]) or simply on matters of fact?

3. Both Lord Walker and Lord Clarke were of the view that a person can be a shadow director *and* a *de facto* director simultaneously. Also see Robert Walker LJ in *Re Kayteck International plc* [1999] 2 BCLC 351 at 424. Is this conceptually possible? How does this square with Millett J's comments in *Re Hydrodam* **[7.01]** ?

[7.03] Re Snelling House Ltd (In Liquidation) [2012] EWHC 440 (Chancery Division)

Liquidators brought proceedings against a former director, and against her husband (R2) who purported to be a consultant to the company, not a director. Mr G Moss QC, applying the principles set out in *Holland* **[7.02]**, found that the husband was a *de facto* director of the company, despite being subject to a 13-year qualification undertaking in relation to another company.

MOSS QC:

24 Although the majority judgments [in *Holland* **[7.02]**] do not provide any precise test applicable to all cases, they provide some helpful guidelines to first instance judges deluged by a mass of reported decisions.

25 Lord Hope at [39] made the following points about the issue:

- Circumstances will vary widely from case to case.
- The question is one of fact and degree.
- There is no single decisive test.
- The purpose of the concept is to impose liability on those in a position to prevent damage to creditors by taking proper steps to protect their interests.
- Those who assume to act as directors and those who thereby exercise the powers and discharge the functions of a director must accept the responsibilities of the office.
- One must look at what the person actually did to see whether he assumed those responsibilities in relation to the subject-matter.

26 Lord Collins also gave helpful guidance at [89] and following:

- Holding out and claiming to be a director are relevant but not necessary factors
- It is impossible to maintain a distinction between de facto and shadow directors
- It is very difficult to identify which functions are the sole responsibility of a director or a board
- The most relevant tests are (a) whether the person was the sole person directing the affairs of the company or at least acting on equal footing with *de jure*directors; (b) holding out by the company and whether the individual used the title of director; (c) whether the individual was part of 'the corporate governing structure'
- Corporate governance means the system by which companies are directed and controlled

27 In the present case, R2 was undoubtedly involved in the day-to-day running of the company … and there is no credible evidence before the Court showing any consultancy. R2's actions in the day-to-day running of the company cannot therefore be explained by reference to such a role.

28 The question remains as to whether the Applicants have overall adduced sufficient evidence to show that R2 was a *de facto* director. In my judgment, they have. …

(p. 318) 30 Along with R1 and R3, R2 was a signatory on the company's account with the bank and had full power under the bank mandate to act in all material respects, including withdrawing the company's

money without any limit. This would have been a surprising power for a mere consultant but would be understandable in the case of a director of a family company.

31 There is no evidence before the Court of any delegation of powers by the sole director, R1, to R2, as one might expect if R2 was involved in the running of the company's affairs otherwise than as director. R2 was also unpaid, which would be very odd for a consultant. There is of course no evidence of any appointment as a consultant.

32 As far as the evidence before the Court goes, R2 did most things that one might expect a director to do in the circumstances in relation to the affairs of the company, and in particular, after the sale of the Company's property, dealt with:

- The resulting VAT issue, and in particular, the claim to repayment of the purchaser of the property, whom R2 successfully fobbed off;
- Withdrawing the Company's monies, in fact for the benefit of himself and/or his family and/or his family company.

'Persons connected with a director': s 252

A person is 'connected with' a director for the purposes, at least, of Pt 10 of the Act and much of the insolvency legislation, in the circumstances laid down by CA 2006 s 252. The people connected with a director are (defined exclusively): members of the director's family, other companies with which the director is 'connected' (ie in which he has, with his 'connected persons', at least a 20% stake), any trustee of a family trust and any partners.

It is important to bear in mind that statutory rules may affect these people as well as the directors. The statutory provisions do not, of course, affect matters at common law (but then the common law has some healthy rules of its own to cope with problems of this sort: see, eg, *Gilford Motor Co Ltd v Horne* **[2.17]** and *Selangor United Rubber Estates Ltd v Cradock* **[10.11]**, although note the following case).

Employees do not, as such, owe fiduciary duties to their employers, although such duties may sometimes be found on the facts. This rule can be crucial in considering the role of senior managers in a company.

[7.04] Ranson v Customer Systems plc [2012] EWCA Civ 841 (Court of Appeal)

An employee started a competing business. His previous employer (CS) alleged breach of fiduciary duties. The trial judge found that Ranson had breached his duties when he failed to inform CS of an opportunity obtained for his own company; when he canvassed for work in competition with CS while still a CS employee; and when he copied details of CS's business contacts, invoices, time sheets and order confirmations for use by his own company. The Court of Appeal (PILL, LLOYD and LEWISON LJJ) disagreed, and allowed the appeal.

LEWISON LJ:

20 It is, at the outset, necessary to distinguish between directors of a company and employees of a company. …

21 The appointment of a person as a company director does not make that person an employee of the company. A director is the holder of an office. Nor does appointment as a company director of itself bring into existence any contract between the director and the company. Many directors will have contracts of service running in parallel with their status as officers of the company. But they are distinct legal relationships.

(p. 319) 22 Whereas a company director will stand in a fiduciary relationship to the company, an employee will not, merely by reason of his role as an employee, assume fiduciary obligations to his employer.

23 In addition as Lord Browne-Wilkinson pointed out in *Henderson v Merrett Syndicates Ltd* [1995] 2 AC