



Guiding businesses through stormy waters

What are my Responsibilities as a Director?

Being a responsible director is a challenge. In addition to using your skills to promote the success of your company, you need to be fully aware of the wide ranging legal obligations and responsibilities which rest firmly on your shoulders as a director.



Failure to meet these obligations could lead to personal liability and ultimately disqualification.

It is also worth remembering that these responsibilities apply to all directors, whether executive or non-executive, and to all types of company whether trading or not. Furthermore, a director can also be liable for the actions of fellow directors.

With this in mind, the following article seeks to highlight the main areas of responsibility and obligation, potential difficulties and how to protect yourself against personal liability.

Statutory Obligations

The 2006 Companies Act sets out seven statutory general duties of directors, these being:

- To act within powers
- To promote the success of the company
- To exercise independent judgement
- To use reasonable care, skill and diligence
- To avoid conflicts of interest
- To not accept benefits from third parties
- To declare an interest in a proposed transaction or arrangement with the company

What does this mean practically?

To act within powers

The powers of a director are defined in the company's constitution or 'Articles of Association'. These are the rules set up at company registration defining how the company is to be run and the powers and responsibilities of its directors. They also outline how decisions are to be made, for example the



procedures for calling a board meeting and the voting process for proposals. They may also place restrictions on directors, for example provisions and restrictions on borrowing by the company.

To promote the success of the company

A director must act in a way that is most likely to promote the success of the company for the benefit of its members as a whole. This will include its shareholders, employees, creditors, customers and suppliers. The impact of the company's operations on the community and environment must also be considered. Furthermore, the long-term prospects and reputation of the company also have to be protected.

To exercise independent judgement

Where roles are delegated, or where external advice is sought, a director needs to demonstrate that his own judgement has been exercised in making decisions and that his power has not been subordinated to the will of others.

To use reasonable care, skill and diligence

A director must demonstrate the levels of skill that can be reasonably expected from a person in that role. For example, a chartered accountant might be expected to know if the company was trading while insolvent.

Using 'reasonable care' as a director might be best explained as the care that one would use in looking after their own affairs.

To avoid conflicts of interest

A director must avoid a situation in which he has a direct or indirect interest that conflicts with the company's interests, for example, if a director has interests in another company with which his company is planning to do business. A conflict of interest may also arise when a director makes personal use of information, property or opportunities belonging to the company.

In the event of a conflict of interest between the company's interests and their own, the directors must always favour the company.

A director is legally obliged to declare any potential or actual conflict of interest to company shareholders.

To not accept benefits from third parties

A director must not exploit his position for personal benefit, or accept benefits (including bribes) which may lead to a conflict of interests.



Company Articles can specify, however, that directors may accept benefits up to a certain level to ensure directors are not in breach of duty just for accepting corporate hospitality.

To declare an interest in a proposed transaction or arrangement

Directors must declare the nature and extent of any interest, direct or indirect, in a proposed transaction with the company before the company enters into that transaction, for example if the person involved in that transaction is a relative, spouse, or partner.

Avoiding getting it wrong

Knowledge and attention to detail are a director's best weapons:

- Be thoroughly familiar with company Articles of Association. Insufficient knowledge of the powers and restrictions of the Articles will inevitably lead to unintentional breaches.
- Remember that the law applies to all directors, whether executive or non-executive, full or part-time.
- Be fully informed of the affairs of the company. It is important to remember that a director can be held liable for the actions of other directors on the board if those actions have occurred through inaction, lack of information or 'turning a blind eye'.
- Be a good record keeper. Regular minuted meetings should always reflect that the correct deliberations have been undertaken before decisions are made. Minuted meetings where there is disagreement over decisions can provide evidence of proper conduct in any legal disagreements.
- Directors should ensure that they are covered by an indemnity insurance policy or professional liability insurance policy. These insurance policies will pay for legal expenses, and sometimes damages if a director is sued for negligence or breach of duty.

What are the Penalties for getting it wrong?

Director responsibilities need to be taken seriously. The penalties for failing to do so can be very great. Ultimately, disqualification or criminal prosecution can result if a director is found to be knowingly fraudulent or deliberately negligent.

Although Directors are not generally liable for the company's debts, being in breach of any of the 7 general statutory duties outlined in the 2006 Companies Act, could lead to a director being held personally liable for any losses to the company that have resulted from his actions or omissions.



Disqualification

Directors need to be aware of the Disqualification Act 1986 which could lead to disqualification from acting as a director of a company for a period of between two and fifteen years.

The Act sets out the criteria by which a director may be judged unfit to manage a company and therefore be disqualified. Disqualification may result from breaches of the general duties of directors, failure to meet statutory obligations, failure to ensure that the company complies with company law, or fraudulent activity.

Those found guilty are liable for fines and, in some cases, imprisonment. If a company has gone through an insolvency process, then the extent of a director's responsibility for that company failure needs to be determined. An adverse conduct report by a liquidator, administrative receiver or administrator could lead to a disqualification.

Other Obligations

Directors are personally responsible for ensuring that the company complies with all aspects of company law. Failing to do so may result in a fine, or in more serious cases disqualification or even imprisonment.

What does this mean practically?

The following responsibilities need to be carried out:

Accounting Records

The 2006 Companies Act requires that proper accounts that are a 'true and fair view' of the business' finances are kept. This includes the preparation of a balance sheet and a profit and loss account for each financial period of the company.

Directors are required to sign a declaration acknowledging their responsibilities with respect to accounting records and the accounts in general.

Statutory Returns

Statutory returns such as the annual report and accounts, the annual return or notification of official company changes to directors or company secretaries must be filed with the Registrar of Companies within the timescales specified by the Companies Act.



Tax

The correct amounts of corporation tax, VAT and National Insurance must be paid on time.

Company documentation

All company business stationery must carry the company name clearly and accurately. In addition to the name, the company's registered number, country of registration and registered address must also appear on its business letters, website, emails and order forms.

The signatory of a company cheque can be personally liable if the company name is not accurately stated.

Employees

Directors are also responsible for ensuring that the company complies with all legislation relating to employees and business premises. For example, a company needs to:

- Comply with employment law with regard to employees – a director can be sued for unfair dismissal, discrimination or unfair work practices. It is important to act quickly to ensure that the company complies with any new legislation.
- Ensure the health and safety of employees – a director will need to undertake a risk assessment of company premises and may need to have a written health and safety policy. A director can be prosecuted for any accident or illness attributed to his negligence.

Avoiding getting it wrong

1. Make sure that company accounting records provide clear, up-to-date financial information at all times. Being equipped with the correct management information will ensure that correct financial decisions or preventative measures can be taken.
2. If the company is in financial difficulty, take steps to minimise the losses to creditors and seek immediate professional help from an insolvency practitioner.
3. Ensure that all statutory records are maintained and all statutory returns are filed on time.
4. Ensuring that the company complies with all legislation relating to employees and business premises.
5. Always seek to avoid or limit personal guarantee of the company's debts.



6. Remember that the law applies to all directors, whether executive or non-executive, full or part-time.
7. Remember that directors can be held liable for the actions of other directors on your board if those actions have occurred through inaction, lack of information or 'turning a blind eye'
8. Directors should ensure that they are covered by an indemnity insurance policy or professional liability insurance policy. These insurance policies will pay for legal expenses, and sometimes damages if a director is sued for negligence or breach of duty.

What are the Penalties for getting it wrong?

Failure to keep accurate accounting records, failure to submit an annual return or failure to notify of changes to statutory information all render a director liable to a fine. On average, more than 1,600 directors are prosecuted each year for failing to deliver this statutory documentation to Companies House on time.

Penalties will also be incurred if deliberate inaccuracies are found in relation to corporation tax or VAT.

A director can also be liable to contribute for company debts incurred through wrongful or fraudulent trading.

In fact, criminal prosecution could result if a director is found to be knowingly fraudulent or deliberately negligent. Materially false, misleading or deceptive accounting records, deliberate tax evasion, fraudulent trading, health and safety shortcomings and misappropriation of company funds are all offences which could result in criminal conviction.

Directors can be personally liable when the duties placed on them by The Health and Safety at Work Act are breached. If a health and safety offence is committed with the consent or connivance of, or is attributable to any neglect on the part of a director, then the director (as well as the organisation) can be prosecuted under section 37 of the Health and Safety at Work Act. Those found guilty are liable for fines or in some cases imprisonment. Health and safety offences are also included in the criteria for disqualification.

Insolvency Obligations

Directors are particularly at risk personally when the company cannot pay its debts, or its liabilities exceed its assets. If a company becomes insolvent, then the extent of a director's responsibility for that company failure needs to be determined.



What does this mean practically?

The Insolvency Act 1986 and the Companies Act 2006 both outline directors' liability with regard to insolvency.

Wrongful trading

A director will be guilty of wrongful trading if he allows the business to carry on and incur debts when knowing there is no reasonable prospect of repaying them.

Fraudulent Trading

A director may be found guilty of fraudulent trading if he allowed the company to trade with intent to defraud creditors.

Avoiding getting it wrong

1. Make sure that company accounting records provide clear, up-to-date financial information at all times. Being equipped with the correct management information will ensure that correct financial decisions or preventative measures can be taken.
2. Take steps to minimise losses to creditors if the company is in, or seems likely to face, financial difficulties.
3. Seek professional advice from an insolvency practitioner to find the best way forward in turning around the business or to decide on the most appropriate informal or formal insolvency procedure.
4. Be a good record keeper. Regular minuted meetings should always reflect that the correct deliberations have been undertaken before decisions are made. Minuted meetings where there is disagreement over decisions can provide evidence of proper conduct in any legal proceedings.

What are the Penalties for getting it wrong?

The potential implications for directors when a company becomes insolvent fall into two categories:

- Personal liability, civil and criminal
- Disqualification



Personal liability

If a director is found guilty of wrongful trading, then the court may declare that the director make a personal contribution to the company's assets. This liability will not apply in circumstances where the director can show that he took every step prior to the liquidation to minimise the potential loss to the company's creditors.

Fraudulent trading is a criminal offence and can be punishable by a fine, imprisonment, or both.

Disqualification

Any liquidator, administrator or administrative receiver appointed to an insolvent company has a duty to report unfit conduct by a director. This can result in a disqualification order being served by the Courts.

Disqualification from acting as a director of a company can last for a period of between two and fifteen years.

This article provides guidance only. Any individual should take professional advice with regard to their particular situation.

MLG Associates are able to provide professional and impartial advice. If you would like to have a free initial consultation regarding your individual circumstances, contact Mike Grieshaber.