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Directors' powers, rights and duties

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Introduction

1. This paper analyses some of the key legal and practical considerations for employment lawyers dealing with cases that involve, or may involve, statutory directors or employees owing fiduciary duties. The paper is broken down into the following topics:

   1.1. Who is a statutory director?

   1.2. Directors' duties under the statutory regime: sections 170 to 177 of the Companies Act 2006 (hereafter referred to as "**the Act**").

   1.3. Directors' authority to act on behalf of the company.

   1.4. Directors' rights to information.

   1.5. Legal advice and considerations of privilege.

   1.6. The practical significance of the distinction between a fiduciary and a 'mere' employee.

   1.7. In what circumstances will fiduciary duties be imposed on employees who are not statutory directors?

   1.8. Remedies for breach of fiduciary duty.

   1.9. Dishonest assistance claims.

   1.10. Derivative claims.

   1.11. Green Paper proposals on strengthening stakeholder voices on company boards.

Who is a statutory director?

2. Put simply, a statutory director is someone who has been appointed a director of a company, in accordance with the provisions of the Act. Part 10, Chapter 1 (ss. 154 – 169) of the Act identifies the legal requirements for appointing, registering and removing a company director.

3. Sections 162 – 167 of the Act stipulate various registration obligations: in summary, each company must maintain an up to date register of its directors which is available for inspection (generally at the company's registered office). In the case of individual directors, s. 163 of the Act stipulates that the following information must be contained within the register:

   3.1. The director's name and any former name

   3.2. A service address;

   3.3. The country or state (or part of the United Kingdom) in which he is usually resident;

   3.4. Nationality;

   3.5. Business occupation (if any); and

   3.6. Date of birth.

4. Section 165 of the Act further provides that every company must keep a register of directors' residential addresses, though this particular register falls outside the scope of the inspection regime described in s. 162 of the Act.

5. Ordinarily, it will be possible to ascertain the identities and service addresses of a company's statutory directors from a simple online search of the UK Companies Register, Companies House. The content of this register is not, however, definitive proof of these matters and may be out of date or otherwise inaccurate (notwithstanding the duty under s. 167 of the Act to notify the registrar of material changes). Prior to taking formal steps in legal proceedings, reasonable steps should be taken to verify

the accuracy of the information contained in the register – for example, submitting a request for inspection of the company's own register (pursuant to s. 162 (5) (b) of the Act).

Directors' duties under the statutory regime: sections 170 to 177 of the Act

6. Part 10, Chapter 2 (ss. 170 – 177) of the Act 'codifies' the general duties of statutory directors, which are defined as follows:

6.1. A duty to act in accordance with the company's constitution and to only exercise powers for the purposes for which they are conferred.

6.2. A duty act in the way the director considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, having regard to (*inter alia*):

6.2.1. the likely consequences of any decision in the long term;

6.2.2. the interests of the company's employees;

6.2.3. the need to foster the company's business relationships with suppliers, customers and others;

6.2.4. the impact of the company's operations on the community and the environment;

6.2.5. the desirability of the company maintaining a reputation for high standards of business conduct; and

6.2.6. the need to act fairly as between members of the company.

6.3. A duty to exercise independent judgment.

6.4. A duty to exercise reasonable care, skill and diligence.

6.5. A duty to avoid a situation in which a situation in which the director has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company. This duty 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).

6.6. A duty not to accept benefits from third parties which are conferred by reason of his being a director, or his doing (or not doing) anything as director (although there will be no breach of duty if the benefit in question cannot reasonably be regarded as likely to give rise to a conflict of interest).

6.7. A duty to declare the nature and extent of any interest the director has in a proposed transaction or arrangement with the company (although there will be no breach of duty if, *inter alia*, that interest cannot reasonably be regarded as likely to give rise to a conflict of interest).

7. Notwithstanding this statutory codification, s. 170 (4) of the Act expressly provides that: "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." It follows that in understanding the nature, extent and application of fiduciary duties, regard must be had to the 'old' case law, as well as case law post-dating the coming into force of the Act.

8. Section 170 (2) makes it clear that the following duties *continue to apply* to a person who has ceased to be a director:

8.1. 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

8.2. Duty not to accept benefits from third parties as regards things done or omitted by him before he ceased to be a director.

<u>Directors' authority to act on behalf of the company</u>

9. Put simply, the actions of a director will bind the company if they had actual or apparent / ostensible authority to enter into a particular transaction or contract etc. on behalf of the company.

10. As to the question of <u>actual</u> authority, the authority to manage the affairs of a company if vested in its board of directors; and a company's constitution / its articles of association will ordinarily identify the general and specific powers bestowed upon individual directors / officers of the company, including the ability to delegate decision-making to appropriate committees etc. Even if directors' particulars area(s) of competence are not expressly laid down in the articles, authority can be implied from the nature of their directorship – for example, a finance director will ordinarily have implied authority to do all such things as fall within the usual scope of that office.

11. However, the fact that a director acts within his general or specific 'area of competence' does not necessarily mean that he had actual authority to bind the company in relation to a particular transaction. This is because, having regard to section 172 of the Act[1], whilst mere negligence on a directors' part will not vitiate a transaction, a director "cannot have actual authority to act in a way which he does not consider, in good faith, to be in the company's interest": **<u>LNOC Limited v Watford Association Football Club Limited</u>** [2013] EWHC 3615 (Comm). As a matter of practical reality, it can be difficult to prove the existence of bad faith.

12. With regard to the issue of <u>apparent / ostensible</u> authority, the key principle of agency law may be summarised as follows: where a reasonable person would understand that an agent has the authority to act on behalf of the principal, the principal will be bound by the agent's acts even if the agent in fact had no actual authority. This may flow from, for example:

    12.1. the appointment of the agent by the principal to a position whose holders *normally* have the relevant authority;

    12.2. representations made by the principal regarding the scope of the agent's authority; and/or

    12.3. dealing with the third party over a period of time, as if the agent were authorised to act on behalf of the principal.

13. However, when considering the issue of apparent / ostensible authority in the context of *directors'* conduct, it is necessary to consider the statutory regime under the Act – in particular:

[1] In short, the duty to act in the best interests of the company.

13.1. By section 43 of the Act, a contract may be made either by some duly authorised person acting on behalf of the company, or by the company itself by writing under its common seal.

13.2. However, by section 40 (1) of the Act, the power of directors to bind a company, or authorise others to do so, is deemed *not* to be constrained by the company's constitution.

13.3. By section 40 (2) (b) of the Act, a third party: (i) is *not* bound to enquire as to any limitation on the powers of the directors to bind the company or authorise others to do so; (ii) is presumed to have acted in good faith unless the contrary is proved; and (iii) is not to be regarded as acting in bad faith by reason *only* of his knowing that an act is beyond the powers of the directors under the company's constitution.

13.4. To establish bad faith in this context, it is therefore necessary to show something additional, such as knowledge of, or being put on inquiry as to, an improper purpose on the part of the directors, or some collusion by the third party in breach by the directors of their duties.

13.5. By section 44 (2), a document (for example a deed) is validly executed by a company if it is signed on behalf of the company by (a) "two authorised signatories"; or (b) "by a director of the company in the presence of a witness who attests the signature".

13.6. By section 44 (3), every director and the company secretary of a company are "authorised signatories".

13.7. By section 44 (4), a document signed in accordance with s 44(2) and expressed, in whatever words, to be executed by the company has the same effect as if it had been executed under the company's common seal.

13.8. Finally, section 44 (5) protects a purchaser in good faith for valuable consideration, where a document purports to have been signed in accordance with section 44 (2) of the Act – i.e. the document is deemed to have been duly executed by the company.

Directors' rights to information

14. Pursuant to section 388 (1) of the Act: "A company's accounting records (a) must be kept at its registered office or such other place as the directors think fit, and (b) must at all times be open to inspection by the company's officers." With regard to the particular type of accounting information a director is entitled to inspect, section 386 of the Act defines what is meant by the maintenance of "adequate accounting records"; in particular, they must contain: (a) entries from day to day of all sums of money received and expended by the company and the matters in respect of which the receipt and expenditure takes place; and (b) a record of the assets and liabilities of the company. In addition, directors have a right to inspect the minutes of board meetings.

15. For their part, members of a company (i.e. shareholders) have (amongst other matters) a statutory right, pursuant to section 229 of the Act, to inspect directors' service contracts with the company or a subsidiary of the company (or, if the contract is not in writing, a written memorandum setting out the terms of the contract).

Legal advice and considerations of privilege

16. When legal proceedings are brought against a company, an individual director of that company may also be named as a personal defendant to the claim. It is a well-known principle that legal advice privilege attaches to communications between a lawyer and the lawyer's *client*, for the purpose of seeking or providing legal advice.[2] In circumstances where: (a) the lawyer's client is identified (for example in the client engagement letter) as the *company only*; (b) there is no basis for implying a joint retainer with the individual director; but (c) legal advice is nevertheless sought and proffered in respect of the claim against the company *and* the individual director, can the individual director (as well as the company) claim privilege over such communications? The answer may yes, by reason of the doctrine of joint interest privilege. In **R (on the application of Stewart Ford) v The Financial Services Authority** [2011] EWHC 2583 (Admin), the High Court held that the FSA acted unlawfully in using material that was protected by legal professional privilege, in an investigation in into the executives of a company, Keydata Investment Services Limited. The High Court accepted that the executives shared with the company joint interest privilege in emails from the company's lawyers, and that the company's

[2] "Legal advice" in this context is to be construed broadly: see for example *Nederlandse Reassurantie Groep Holding NV ('NRG') v Bacon & Woodrow* [1995] 1 All ER 976.

administrators had not been entitled to waive privilege on their behalf. At paragraph 40 of the judgment, Burnett J summarised the key principles as follows:

> "In my judgment…an individual claiming joint privilege with others in a communication with a lawyer, when there is no joint retainer, will need to establish the following facts by evidence:
>
> i) That he communicated with the lawyer for the purpose of seeking advice in an individual capacity;
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> ii) That he made clear to the lawyer that he was seeking legal advice in an individual capacity, rather than only as a representative of a corporate body;
>
> iii) That those with whom the joint privilege was claimed knew or ought to have appreciated the legal position;
>
> iv) That the lawyer knew or ought to have appreciated that he was communicating with the individual in that individual capacity.
>
> v) That the communication with the lawyer was confidential."

17. Joint privilege can only be waived with the consent of all the parties to whom that privilege attaches.

18. In circumstances where a company is in a dispute or litigation (or envisages a dispute or litigation) with one of its directors, it may wish to seek legal advice and is unlikely to want the aggrieved director to have access to that legal advice. In this scenario, it is particularly important for the lawyers and the company to:

    18.1. identify, with precision, which individual(s) is charged with seeking the advice (and is to be regarded as "the client" for this purpose);

    18.2. the purpose for which the advice is sought (which may be in conflict with the personal interests of the individual director); and

    18.3. carefully limit the circulation and/or dissemination of the advice within the company, so as to avoid arguments that privilege has been waived (vis-à-vis the individual director) by reason of a loss of confidentiality in the advice.

<u>The practical significance of the distinction between a fiduciary and a 'mere' employee</u>

19. As explained below, the practical significance of establishing the existence of fiduciary duties on the part of an employee will often boil down to two issues:

    19.1. Establishing liability in circumstances where the conduct complained of would not ordinarily amount to a breach of the employee's contract of employment; and

    19.2. Broadening the innocent party's options in terms of available remedies.

20. With regard to the first issue, contracts of employment will always include express and/or implied terms of loyalty, fidelity and mutual trust and confidence. Notwithstanding the significance of these terms, it is possible for an employee to act consistently with those contractual duties but nevertheless commit a breach of fiduciary duty.

21. With regard to the second issue, advancing a case by reference to breach of fiduciary duty will give rise to claims for equitable relief, including an account of profits, and may allow an innocent party to 'side-step' potentially difficult issues regarding loss, causation and remoteness.

<u>In what circumstances will fiduciary duties be imposed on employees who are not statutory directors?</u>

22. In the context of employment disputes, particularly those involving 'poaching raids' or 'team moves', the question will often be posed: 'is Employee X a fiduciary or not?' If the employee is also a statutory director of the company, the answer to that question is straightforwardly yes, and the whole range of fiduciary duties listed above will operate to regulate that employee's conduct.

23. More often, however, the employee(s) accused of improper conduct are senior employees but not statutory directors. As explained in this paper, asking the question 'is Employee X a fiduciary or not?', in the sense of a binary, all or nothing state of affairs, can be an unhelpful way of analysing the issue. As illustrated below, an employee may well owe fiduciary obligations in respect of some but not all of his day to day work and contractual duties.

24. In **<u>Nottingham University v Fishel & another</u>** [2000] IRLR 471, in analysing the distinction that is properly to be drawn between employment and fiduciary duties, Elias J made the following observations (emphasis added):

> "86…circumstances may arise in the context of an employment relationship, or arising out of it, which, when they occur, will place the employee in the position of a fiduciary. In Blake itself, as I have indicated, it was the receipt of confidential information. There are other examples. Thus every employee is subject to the principle that he should not accept a bribe and he will have to account for it (and possibly any profits derived from it) to his employer…But his fiduciary obligations are limited and arise out of the particular circumstances…
>
> 90… the essence of the employment relationship is not typically fiduciary at all. Its purpose is not to place the employee in a position where he is obliged to pursue his employer's interests at the expense of his own. The relationship is a contractual one and the powers imposed on the employee are conferred by the employer himself. The employee's freedom of action is regulated by the contract, the scope of his powers is determined by the terms (express or implied) of the contract, and as a consequence the employer can exercise (or at least he can place himself in a position where he has the opportunity to exercise) considerable control over the employee's decision-making powers.
>
> 91 This is not to say that fiduciary duties cannot arise out of the employment relationship itself. But they arise not as a result of the mere fact that there is an employment relationship. Rather **they result from the fact that within a particular contractual relationship there are specific contractual obligations which the employee has undertaken which have placed him in a situation where equity imposes these rigorous duties in addition to the contractual obligations. Where this occurs, the scope of the fiduciary obligations both arises out of, and is circumscribed by, the contractual terms**; it is circumscribed because equity cannot alter the terms of the contract validly undertaken.
>
> 92 The problem of identifying the scope of any fiduciary duties arising out of the relationship is particularly acute in the case of employees…There are many cases which have recognised the existence of the employee's duty of good faith, or loyalty, or the mutual duty of trust and confidence – concepts which tend to shade into one another...Unfortunately, these concepts are frequently used in the employment context to describe situations where a party merely has to take into consideration the interests of another, but does not have to act in the interests of that other…
>
> 95… The duty of trust and confidence limits the employer's powers, but it does not require him to act as a fiduciary. It is a contractual but not a fiduciary obligation.

> 96… Accordingly, in analysing the employment cases in this field, care must be taken not automatically to equate the duties of good faith and loyalty, or trust and confidence, with fiduciary obligations...
>
> 97 **Accordingly, in determining whether a fiduciary relationship arises in the context of an employment relationship, it is necessary to identify with care the particular duties undertaken by the employee, and to ask whether in all the circumstances he has placed himself in a position where he must act solely in the interests of his employer. It is only once those duties have been identified that it is possible to determine whether any fiduciary duty has been breached**.
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> 98 It follows that fiduciary duties may be engaged in respect of only part of the employment relationship, as was recognised by Lord Wilberforce, giving judgment for the Privy Council in *New Zealand Netherlands Society v Kuys* [1973] 1 WLR 1126 at 1130:
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>> 'A person ... may be in a fiduciary position quoad a part of his activities but not quoad other parts: each transaction, or group of transactions, must be looked at.'"

25. These statements of principle have been endorsed in numerous other cases, including by the Court of Appeal in **<u>Helmet Integrated Systems Limited v Tunnard</u>** [2007] IRLR 126.

26. In determining whether or not an employee is also a fiduciary, and if so precisely what fiduciary duties are owed by that employee to his employer, relevant factors may include some or all of the following:

    26.1. How the employee's role and responsibilities are described in the contractual documentation;

    26.2. The seniority of the employee within the company (although, as noted below, relatively junior employees may still owe fiduciary duties in certain circumstances);

    26.3. The degree of autonomy entrusted to the employee;

    26.4. The degree of influence that the employee enjoys vis-à-vis colleagues and third parties (clients, customers, suppliers etc);

26.5. The extent to which the employee is involved in the formulation of policy and strategy for the company;

26.6. The extent to which the employee carries out functions in relation to the company which could properly be discharged only by a director and/or is held out as a director by the company (with the employee's knowledge and/or approval) – e.g. when seeking investment from third parties;

26.7. The nature and extent of confidential information / trade secrets entrusted to the employee (misuse of which would render the employer particularly vulnerable);

26.8. The extent to which the employee's salary and/or bonus is directly linked to the turnover and/or profits of the company;

26.9. The existence and nature of any express obligations in the contract of employment vis-à-vis the reporting of competitive activity / threats etc;

26.10. Generally accepted practices within the particular industry / sector under consideration – e.g. the extent to which consultancy work for third parties is permitted and/or encouraged by other employers in that field (see **Fishel**).

27. Some examples of specific fiduciary duties that Courts have and have not been willing to identify / impose on 'mere' employees, having regard to the particular facts of the cases, are given below:

27.1. In **Fishel**, the High Court held that the defendant (an eminent scientist employed by Nottingham University) did *not* owe any fiduciary duties in respect of the paid work that he personally carried out in private clinics abroad. Significantly, he was under "no contractual obligation to seek to obtain work abroad of this nature on behalf of the university, nor in my opinion could he have been contractually obliged to do the work abroad that he did…If Dr Fishel had done work of this kind in his spare time, I doubt whether the university would, or could, have alleged that he was infringing any duty, not even the contractual duty not to compete, since these clinics abroad were not competitors."

27.2. However, the Court held that Dr Fishel *did* owe a fiduciary duty not to deploy university staff members to carry out work for the private clinics based abroad. *Per* Elias J: "Dr Fishel also profited from the fact that he was paid for work done by other embryologists for whom he was responsible. In my opinion, this activity has to be seen in a different light to his own activities abroad. It was his duty to direct the other embryologists what to do and where to do it. By accepting work for them from which he was directly benefiting, he was in my view clearly putting himself where there was a potential conflict between his specific duty to the university to direct the embryologists to work in the interests of the university, and his own financial interest in directing them abroad. The fact that he did not in fact act contrary to the interests of the university is irrelevant: it is trite law that the potential conflict is enough."

27.3. In **Shepherds Investments Limited v Walters & others** [2006] EWHC 836, all three individual defendants (one of whom was *not* a statutory director of the claimant) were held to be in breach of their fiduciary duties to their employer (including the duty to avoid conflicts of interest) from the point in time when they formed an irrevocable intention to establish a business which they knew would fairly be regarded as a competitor company, without providing full disclosure of all material facts.

27.4. In **Helmet v Tunnard**, the Court of Appeal held that Mr Tunnard: (a) did *not* owe a fiduciary duty to disclose his *own* preparations, outside of working hours, for engaging in competitive activity post-employment (including raising funds for a new project); but (b) having regard to the express terms of his contract of employment, *did* owe a fiduciary duty to disclose information which came to his attention regarding the intentions of third parties to compete with his employer (albeit he had not breached that particular obligation on the facts).

27.5. In **National Grid v McKenzie** [2009] EWHC 1817, the High Court held that a project engineer (who was a relatively junior employee) did owe fiduciary duties in relation to specific elements of his work and conduct – namely the negotiation and awarding of particular contracts on behalf of his employer. This was so, notwithstanding the fact that Mr McKenzie did not have the authority to award or enter into certain contracts on behalf of his employer without first obtaining a countersignature from a more senior colleague.

27.6. In **Ranson v Customer Systems Plc** [2012] EWCA Civ 841, the Court of Appeal held that Mr Ranson did *not* owe any fiduciary duty to disclose the fact that he was preparing to compete with his employer post-termination, or to report meetings he had had with clients of his employer, which had taken place at a time when Mr Ranson was taking preparatory steps to compete.

27.7. In **QBE Management Services (UK) Limited v Dymoke & others** [2012] IRLR 458, the Court held that a senior employee, who was not a statutory director, *did* owe fiduciary duties to his employer (in the context of a 'team move' situation). The factors which led the Court to reach this conclusion included the following:

27.7.1. Mr Dymoke played a pivotal role in the protection and indemnity ("P&I") part of the claimant's marine insurance business;

27.7.2. He was responsible for all the P&I underwriters, including Mr Hearn (the second defendant), and was equivalent to a desk head;

27.7.3. He had been a statutory director of the company which was the original employer of the British Marine staff, British Marine Management Ltd;

27.7.4. He was the most senior executive within the British Marine Business after the head of British Marine and its chairman;

27.7.5. The company placed a high level of trust in him. He was the sole P&I representative on the divisional management committee and was given access to sensitive business information – in particular: quarterly accounts, financial performance information, claims data and information relating to broker relationships and performance against targets; and

27.7.6. He was also involved in developing and implementing QBE's strategic business plans.

27.8. In the circumstances, the Court held that Mr Dymoke owed three principal fiduciary duties to his employer:

27.8.1. A duty to act in good faith in the best interests of the claimant, which included, as an incidence thereof, a positive duty to inform the claimant in a timely manner of any activity, actual or threatened, which might damage the claimant's interests;

27.8.2. A duty to use his best endeavours to promote and protect the interests of the group of companies of which the claimant formed part; and

27.8.3. A duty not to place himself in a position in which his interests, or any duties owed by him to any third party, might conflict with the interests or duties owed by him to the claimant.

27.9. In **Airbus Operations Limited v Withey** [2014] EWHC 1126, the Court held that Mr Whitney did owe fiduciary duties in relation to a procurement process over which he had a considerable degree of influence. In particular, he owed fiduciary duties in respect of:

27.9.1. Directing the work of the teams under him;

27.9.2. Administering specific budgets, which included giving his approval of quotations for work within his area of responsibility;

27.9.3. Any intervention he made in the procurement process which determined or influenced (in the sense that the decision might have been different without his intervention) what work was awarded to whom at what cost;

27.9.4. A duty not to be engaged in any capacity in another business in any way which might conflict with the best interests of Airbus, unless specific and informed approval was given; and

27.9.5. A duty to disclose any such engagement which would contravene the duty identified in paragraph 17.9.4 above.

28. It is also important to note that it in order to avoid liability for breach of fiduciary duty, it is insufficient for a defendant to show that the principal (in employment disputes, the employer) had some knowledge of the defendant's wrongful conduct, or should have known about it. In **Hamilton v Campbell** [2015] S.C.L.R. 17, the Court of Session held that:

> "Informed consent requires that the principal should be in full possession of all material facts…the principal himself must be aware of the facts. Furthermore, the principal must understand fully what the proposals are; in particular, he must understand his legal rights under the fiduciary relationship and in what way those rights are to be given up. Once again, it is essential that the principal himself should be aware of all of these factors and apply his mind to them. The knowledge and understanding of an agent for the principal are not sufficient. The only exception to this would arise in a case where such an agent was empowered by the principal to undertake dealings with the fiduciary on the principal's behalf, as where a solicitor was specifically empowered to authorise the fiduciary to take remuneration. It is difficult to imagine that such a case could arise otherwise than by clear instructions to the solicitor, however, as the application of fiduciary duties is an important matter and the principal must understand that he is authorising the abrogation of such duties…"

Remedies for breach of fiduciary duty

29. Section 178 of the Act provides as follows:

> "**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."

30. In **National Grid v McKenzie**, the High Court summarised the position regarding remedies for breach of fiduciary duty as follows:

"The remedy to be fashioned for breach of fiduciary duty must be one that is fair in all the circumstances, depriving the defaulting fiduciary of all benefit derived from the transaction, but not otherwise punishing him."

31. In **Philip Towers v Premier Waste Management** [2012] IRLR 73, the High Court held that liability to pay compensation for breach of fiduciary duty:

> "… does not depend on proof of fault or proof that the conflict of interest has in fact caused the company loss…A director's potential conflict of interest may arise, for example, in connection with a business opportunity. If a director obtains the opportunity for himself, he will be liable to the company for breach of duty regardless of the fact that he acted in good faith or that the company could not, or would not, take advantage of the opportunity."
>
> "Equity's response of strict liability to account for breach of a fiduciary duty is similar whether the liability is triggered by an event which breaches the loyalty duty, or the 'no conflict principle', or the 'no profit principle."

32. In **FHR European Ventures v Cedar Capital Partners** [2014] UKSC 45, the Supreme Court approved the "well established principle", derived from *Regal (Hastings) Ltd v Gulliver (Note)* [1942] 1 All ER 378, that liability to account for the profits or benefit obtained from a breach of fiduciary duty:

> "… 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 benefitted by his action. Liability arises from the mere fact of 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."

33. **Murad v Al-Saraj** [2005] EWCA Civ 959 is a good example of what may be regarded as the 'harshness' of this principle. In this case, as part of a joint venture arrangement, the defendant, Mr Al-Saraj, represented that he would contribute £500,000 towards the £4.1 million cost of acquiring a hotel. In fact he did not do so, instead setting off an unenforceable debt that the seller of the property owed him. In addition, the defendant received a commission of £369,000 for arranging the sale, which he failed to disclose. The hotel was subsequently sold at a profit of $2m. Under the joint venture agreement, the parties were entitled to a 50:50 share of any capital profit from the onward sale of the hotel.

34. Having regard to the High Court's finding that the defendant had fraudulently misrepresented his contribution to the purchase price and had acted in breach of fiduciary duty, the Court of Appeal considered the issue of account of profits. The defendant's appeal proceeded on the basis that (*inter alia*):

34.1. Had there been no misrepresentation, the joint venture would still have proceeded as it did; and

34.2. An account of all the profits made by him did not reflect the extent of his wrongdoing and would result in the unjust enrichment of the claimants.

35. These arguments were unsuccessful. The Court of Appeal made a stringent order for an account of profits (albeit Clarke LJ dissented on the extent of Mr Al-Saraj's liability to account), holding that a party is liable to account:

35.1. Whether or not the claimant would have been able to generate the profit made by the defendant; and

35.2. Even where the defendant's unlawful act did not affect the outcome.

36. In her judgment, Arden LJ observed at para. 74:

> "It may be asked why equity imposes stringent liability of this nature. The passage just cited from the judgment of Lord Eldon LC makes it clear that equity imposes stringent liability on a fiduciary as a deterrent… in the interests of efficiency and to provide an incentive to fiduciaries to resist the temptation to misconduct themselves, the law imposes exacting standards on fiduciaries and an extensive liability to account."

37. In summary, in assessing the value of an account of profits:

37.1. The starting point is that the defendant is liable to account for the full value of the profit made, regardless of what would have happened but for the breach of fiduciary duty;

37.2. It is for the defendant to show why it would be inequitable to order an account of all the profits;

37.3. There may be a reduction in the amount for which the defendant has to account, where it can be shown that an element of the profit is *attributable to the defendant's skill and effort*.

38. In **Helmet v Tunnard**, the Court of Appeal emphasised that one reason why care must be taken "not to equate the duty of good faith and loyalty owed by every employee with a fiduciary obligation" is because:

> "Unless that distinction is maintained common law rules of causation and remoteness of damages may be 'miraculously sidestepped by intoning the magic formula (breach of fiduciary duty)' (see Lord Millett in '*Equity's Place in the Law of Commerce*' (1998) 114 LQR 214 at 217)."

39. Put simply, electing for an account of profits, rather than damages or an inquiry as to damages, is likely to benefit a claimant which finds itself in a position where:

39.1. The claimant has suffered no actual loss as a result of the breach of fiduciary duty – for example, the scenario in which a business opportunity that has been diverted by the defendant in breach of fiduciary duty would not have come to fruition (for the claimant), even if the fiduciary had acted in accordance with his duties;

39.2. The claimant is likely to face significant evidential and legal hurdles in proving the nature and extent of the damage it has suffered as a result of the breach of fiduciary duty; and/or

39.3. The profits wrongfully received by the defendant exceed the profits that would have been received by the claimant, had there been no breach of fiduciary duty.

40. With regard to the question of election, in **Tang Man Sit v Capacious Investments Limited** [1996] AC 514, the House of Lords held as follows:

"Faced with alternative and inconsistent remedies a plaintiff must choose, or elect, between them. He cannot have both. The basic principle governing when a plaintiff must make his choice is simple and clear. He is required to choose when, but not before, judgment is given in his favour and the judge is asked to make orders against the defendant. A plaintiff is not required to make his choice when he launches his proceedings. He may claim one remedy initially, and then by amendment of his writ and his pleadings abandon that claim in favour of the other. He may claim both remedies, as alternatives. But he must make up his mind when judgment is being entered against the defendant.

41. Lord Nicholls went on to explain that:

"In the ordinary course, by the time the trial is concluded a plaintiff will know which remedy is more advantageous to him. By then, if not before, he will know enough of the facts to assess where his best interests lie. There will be nothing unfair in requiring him to elect at that stage. Occasionally this may not be so. This is more likely to happen when the judgment is a default judgment or a summary judgment than at the conclusion of a trial. A plaintiff may not know how much money the defendant has made from the wrongful use of his property. It may be unreasonable to require the plaintiff to make his choice without further information. To meet this difficulty, the court may make discovery and other orders designed to give the plaintiff the information he needs, and which in fairness he ought to have, before deciding upon his remedy. A recent instance where this was done is the decision of Lightman J in *Island Records Ltd v Tring International plc* [1995] 3 All ER 444. The court will take care to ensure that such an order is not oppressive to a defendant…"

42. The harshness of the 'strict liability' principle to account for breach of fiduciary duty may, in some circumstances, be mitigated or avoided by virtue of s. 1157 of the Act, which provides as follows:

"**1157 Power of court to grant relief in certain cases**

(1) If in proceedings for negligence, default, breach of duty or breach of trust against—

(a) an officer of a company, or

(b) a person employed by a company as auditor (whether he is or is not an officer of the company),

it appears to the court hearing the case that the officer or person is or may be liable but that he acted honestly and reasonably, and that having regard to all the circumstances of the case (including those connected with his appointment) he ought fairly to be excused, the court may relieve him, either wholly or in part, from his liability on such terms as it thinks fit.

> (2) If any such officer or person has reason to apprehend that a claim will or might be made against him in respect of negligence, default, breach of duty or breach of trust—
>
> > (a) he may apply to the court for relief, and
> >
> > (b) the court has the same power to relieve him as it would have had if it had been a court before which proceedings against him for negligence, default, breach of duty or breach of trust had been brought.
>
> ….

43. In essence, s. 1157 of the Act provides the Court with a statutory basis on which it may legitimately disapply the equitable rules that would ordinarily apply to the assessment of remedy, in circumstances where a breach of fiduciary duty has been established. It is important to note, however, that this provision may only be prayed in aid by statutory officers of companies, and not 'mere' employees who are found to owe fiduciary duties to their employer (save for the limited 'auditor exception' in s. 1157 (1) (b) of the Act).

44. One interesting issue that recently arose for consideration is whether a successful claimant may seek an order from the Court that a bribe / secret commission obtained by a defendant in breach of fiduciary duty are held *on trust* for the claimant, or whether the innocent party's only claim is for equitable compensation. In **FHR European Ventures v Cedar Capital Partners**, the Supreme Court confirmed that a *proprietary* remedy (i.e. a declaration that money is held by the defendant on trust for the claimant) is permissible. It approved a principle of law that "any benefit acquired by an agent as a result of his agency and in breach of his fiduciary duty is held on trust for the principal." The practical significance of this legal principle is that the innocent party has a right to trace and follow the proceeds that have wrongfully been obtained by the fiduciary and passed into the hands of knowing recipients.

45. Another equitable remedy potentially available to a successful claimant is the *rescission* of a contract(s) concluded by a defendant a breach of fiduciary duty. This is a discretionary remedy and will not be granted by the Court where it would be unfair and disproportionate to do so: see for example **Hurstanger Limited v Wilson & another** [2007] EWCA Civ 299.

Dishonest assistance claims

46. The essential legal principle was articulated by Andrew Smith J in **Trust & Holding Corp v Privalov** [2010] EWHC 3199 (Comm) as follows:

> "A defendant is liable for procuring or assisting in a breach of trust or fiduciary duty if a person acted in breach of a fiduciary duty owed to the claimant, and the defendant dishonestly persuaded that person to do so or assisted him to do so. … It is not necessary that the breach of duty should involve property held on trust or its misapplication or misappropriation…"

47. As to what is meant by "assistance" in this context, in **Baden v Société Générale pour Favoriser le Développement du Commerce et de l'Industrie en France SA** [1993] 1 WLR 509, Peter Gibson J held (albeit in a non-employment context):

> "…it seems to me to be a simple question of fact, whether or not there has been assistance. The payment by a bank on the instructions of fraudulent directors of a company of moneys of the company to another person may be such assistance, as in the Selangor case [1968] 1 WLR 1555 and the Karak case [1972] 1 WLR 602. Mr Leckie submitted that there cannot be assistance for the purposes of constructive trusteeship unless that which is done by the stranger inevitably has the consequence that a loss is suffered and that a mere payment which in itself does not have that consequence is not sufficient. I accept that the assistance must be an act which is part of the fraudulent and dishonest design and must not be of minimal importance but I am not aware of any reasons of principle or by way of authority why Lord Selborne LC's test should bear the further gloss which Mr Leckie would put on it."

48. As to what is meant by "dishonest" assistance in this context, this matter was considered by the House of Lords in **Twinsectra Ltd v Yardley** [2002] UKHL 12. Lord Hutton described the three possible standards which can be applied to determine whether a person has acted dishonestly:

    48.1. A purely subjective standard whereby a person is only regarded as dishonest if he transgresses his own standard of honesty even if that standard is contrary to that of reasonable and honest people;

    48.2. A purely objective standard whereby a person acts dishonestly if his conduct is dishonest by ordinary standards of reasonable and honest people, even if he does not realise this; and

    48.3. A combined standard, which combines an objective test and a subjective test, and which requires that before there can be a finding of dishonesty it must be established that the defendant's conduct was dishonest by the ordinary standards of reasonable and honest people and that he himself realised that by those standards his conduct was dishonest. This is akin to the 'Ghosh test'[3] that is applied in criminal cases, including prosecutions under the Theft Act 1968 and the Fraud Act 2006.

49. Lord Hutton (with whose speech the majority of their Lordships agreed) concluded that dishonesty in this context should be assessed by reference to the 'combined standard', namely that:

49.1. The third party must have knowledge that what he was doing would be regarded as dishonest by honest people; although

49.2. He should not escape a finding of dishonesty because he sets his own standards of honesty and does not regard as dishonest what he knows would offend the normally accepted standards of honest conduct.

50. For his part, in **Twinsectra Ltd v Yardley**, Lord Hoffman held that a dishonest state of mind means "consciousness that one is transgressing ordinary standards of honest behaviour."

51. This issue was reconsidered by the Privy Council in **Barlow Clowes International Ltd v Eurotrust International Ltd** [2005] UKPC 37. Lord Hoffman held as follows:

> "[15] Their Lordships accept that there is an element of ambiguity in [Lord Hutton's] remarks which may have encouraged a belief, expressed in some academic writing, that Twinsectra had departed from the law as previously understood and invited inquiry not merely into the defendant's mental state about the nature of the transaction in which he was participating but also into his views about generally acceptable standards of honesty. But they do not consider that this is what Lord Hutton meant. The reference to "what he knows would offend normally accepted standards of honest conduct" meant only that his knowledge of the transaction had to be such as to render his participation contrary to normally acceptable standards of honest conduct. It did not require that he should have had reflections about what those normally acceptable standards were.
>
> [16] Similarly in the speech of Lord Hoffmann, the statement (in para 20) that a dishonest state of mind meant "consciousness that one is transgressing ordinary standards of honest behaviour" was in their Lordships' view intended to require

[3] Derived from **R v Ghosh** [1982] QB 1053

consciousness of those elements of the transaction which make participation transgress ordinary standards of honest behaviour. It did not also to require him to have thought about what those standards were."[4]

52. It follows that, *per* the Privy Council in **Barlow Clowes**, subjective knowledge of the alleged 'dishonest assistant' is a necessary component of the equitable wrong, in respect of certain *factual* matters – specifically, those "elements of the transaction" which, viewed objectively, it would have been dishonest to participate in / assist with. However, it is not necessary for the claimant to prove that the defendant was subjectively aware or conscious of ordinary standards of honesty in the relevant context.

53. At para. 10 of his speech in **Barlow Clowes**, Lord Hoffman articulated the relevant law on "dishonest assistance" as follows:

> "The judge stated the law in terms largely derived from the advice of the Board given by Lord Nicholls of Birkenhead in *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378, [1995] 3 All ER 97. In summary, she said that liability for dishonest assistance requires a dishonest state of mind on the part of the person who assists in a breach of trust. Such a state of mind may consist in knowledge that the transaction is one in which he cannot honestly participate (for example, a misappropriation of other people's money), or it may consist in suspicion combined with a conscious decision not to make inquiries which might result in knowledge: see *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd* [2001] UKHL 1, [2003] 1 AC 469, [2001] 1 All ER 743. Although a dishonest state of mind is a subjective mental state, the standard by which the law determines whether it is dishonest is objective. If by ordinary standards a defendant's mental state would be characterised as dishonest, it is irrelevant that the defendant judges by different standards. The Court of Appeal held this to be a correct state of the law and their Lordships agree."

54. In **Abou-Rahmah and Others v Abacha and Others** [2006] EWCA Civ 1492 CA, Rix LJ noted the uncertainty regarding the nature of the "dishonest assistance" test in this context, stating:

> "[16] Without intending or attempting myself to restate the authorities, I would merely hazard this analysis. It would seem that a claimant in this area needs to show three things: first, that a defendant has the requisite knowledge; secondly,

[4] That was so, notwithstanding that in para. 20 of Lord Hoffman's speech in **Twinsectra**, he had actually stated: "…I consider that those principles [in *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378] require more than knowledge of the facts which make the conduct wrongful. They require a dishonest state of mind, that is to say, consciousness that one is transgressing ordinary standards of honest behaviour."

that, given that knowledge, the defendant acts in a way which is contrary to normally acceptable standards of honest conduct (the objective test of honesty or dishonesty); <u>and thirdly, possibly</u>, that the defendant must in some sense be dishonest himself (a subjective test of dishonesty which might, on analysis, add little or nothing to knowledge of the facts which, objectively, would make his conduct dishonest)"

[17] It is the third element which raises a problem of definition in the light of *Twinsectra* and *Barlow Clowes*…" (Underlining added)

55. Having identified this "controversy", Rix LJ held that he did not need to determine it for the purpose of the appeal in Abou-Rahmah. Arden LJ did, however, express a clear view on this issue; she held (at para. 65):

"The…decision of the House of Lords in *Twinsectra Ltd v Yardley* [2002] UKHL 12, [2002] 2 AC 164, [2002] 2 All ER 377 was widely interpreted as requiring both an objective and subjective test to be applied to the question of standard. In the case of the subjective test, that would mean that the Defendant would not be guilty of dishonesty unless he was conscious that the transaction fell below normally acceptable standards of conduct. The Privy Council in the *Barlow Clowes* case has now clarified that this is a wrong interpretation of the *Twinsectra* decision. It is not a requirement of the standard of dishonesty that the defendant should be conscious of his wrongdoing. *Snell's Equity* now refers to this as the 'better view' (31st ed, para 28–46 as updated)."

56. Arden LJ went on to hold (at para. 59 (a)):

"…In *Barlow Clowes International Ltd (in liquidation) v Eurotrust International Ltd* [2006] 1 All ER 333, the Privy Council considered the case law of England and Wales on the issue of the element of dishonesty necessary for liability under this head. Its interpretation of that case law was that it is unnecessary to show subjective dishonesty in the sense of consciousness that the transaction is dishonest. It is sufficient if the defendant knows of the elements of the transaction which make it dishonest according to normally accepted standards of behaviour. This is the first opportunity, so far as I am aware, that this court has had an opportunity of considering the decision of the Privy Council, and in my judgment this court should follow the decision of the Privy Council..."

57. Pill LJ acknowledged (at para. 94 in <u>**Abou-Rahmah**</u>) the value of <u>**Barlow Clowes**</u> in its explanation of <u>**Twinsectra**</u>. He considered that its implications should await further consideration in a case in which a real issue arose on its impact.

58. In **Starglade Properties Ltd v Roland Nash** [2010] EWCA Civ 1314, the Court of Appeal considered the authorities referred to above and held as follows (*per* Sir Andrew Morritt at para. 32):

> "The relevant standard, described variously in the statements I have quoted, is the ordinary standard of honest behaviour. Just as the subjective understanding of the person concerned as to whether his conduct is dishonest is irrelevant so also is it irrelevant that there may be a body of opinion which regards the ordinary standard of honest behaviour as being set too high. Ultimately, in civil proceedings, it is for the court to determine what that standard is and to apply it to the facts of the case."

59. Applying this principle to the facts of **Starglade**, Sir Andrew Moritt held (at para. 40):

> "I would accept the first submission of counsel for Starglade and, notwithstanding those of counsel for Mr Nash, recognise the conduct of Mr Nash in assisting the undoubted breach of trust in favour of Starglade as dishonest by the ordinary standards of honest commercial behaviour."

60. Thus, the position now appears to be settled: the principles articulated by the Privy Council in **Barlow Clowes** are those to be applied when considering the question of dishonest assistance in this context.

61. Once liability for dishonest assistance has been established, the focus turns to remedy. Until relatively recently, there was uncertainty as to the scope of the remedies available against a third party found to have dishonestly assisted in a breach of fiduciary duty. In **Novoship (UK) Limited & others v Niktin & others** [2014] EWCA Civ 908, the Court of Appeal held that a claimant *is* entitled to seek an account of profits against the dishonest assister, even though: (a) they are not themselves a fiduciary and (b) no loss has been suffered.

62. In **Novoship**, Longmore LJ held (at paras. 74 – 75):

> "[74] …The way in which (at least in recent times) the liability of a dishonest assistant has been described is "accountable in equity": *Paragon Finance plc v D B Thakerar & Co* [1999] 1 All ER 400 at 409; *Dubai Aluminium Co Ltd v Salaam* [2002] UKHL 48; [2003] 2 AC 366 at para 141. In the latter case Lord Millett said:
>
> > 'Equity gives relief against fraud by making any person sufficiently implicated in the fraud accountable in equity. In such a case he is traditionally (and I have suggested unfortunately) described as a 'constructive trustee' and is said to be 'liable to account as a constructive

trustee'. But he is not in fact a trustee at all, even though he may be liable to account as if he were. He never claims to assume the position of trustee on behalf of others, and he may be liable without ever receiving or handling the trust property.'

[75] It is true that the phrase 'accountable in equity' does not expressly answer the question: accountable for what? But if the limit of a dishonest assistant's liability is a liability to make good losses suffered by the beneficiary it is an odd phrase to use. We agree with *Snell's Equity* (32nd ed §30-079) that, subject to one qualification to which we will come, both a liability to make good loss and a liability to account for profits 'follow from the premise that the defendant is held liable to account as if he were truly a trustee to the claimant.'"

63. Longmore LJ summarised the position thus (at para. 84):

"…Where, as here, the equitable wrong is itself linked with a breach of fiduciary duty we see no reason why a court of equity should not be able to order the wrongdoer to disgorge his profits in so far as they are derived from the wrongdoing."

64. The "one qualification" foreshadowed by Longmore LJ in para. 75 of his judgment relates to the Court's discretion *not* to order an account of profits against a dishonest assistant, in circumstances where the Court deems that remedy to be disproportionate in relation to the particular form and extent of the dishonest assistant's wrongdoing. Longmore LJ articulated the distinction between fiduciaries and dishonest assistants in this respect as follows:

"[116] …What the ship owning companies wanted to do was to charter their vessels on time charters at market rates. That is what they achieved. As Arden LJ put it in *Murad* at para 85:

"The kind of account ordered in this case is an account of profits, that is a procedure to ensure the restitution of profits which ought to have been made for the beneficiary and not a procedure for the forfeiture of profits to which the defaulting trustee was always entitled for his own account."

[117] Since the ship owning companies wished to avoid the risk of fluctuating rates for freight, and wished to secure a long term income, they necessarily wished to lay off the risk on to the charterer. Thus the profits that Mr Nikitin in fact made were the kind of profits that the ship owning companies deliberately decided to forgo. In our judgment they cannot be described as profits which ought to have been made for the beneficiary, and therefore they fall outside the rationale for the ordering of an account.

> [118] Mr Brindle relied on the inflexible rule of equity that where a fiduciary has made an unauthorised profit within the scope of his duty he is bound to account for it to his principal. We do not wish to cast any doubt on that well-established principle. But at the risk of tedium we repeat that Mr Nikitin was not a fiduciary and is not sued for any breach of fiduciary duty.
>
> [119] We consider that where a claim for an account of profits is made against one who is not a fiduciary, and does not owe fiduciary duties then, as Lord Nicholls said in *Blake*, the court has a discretion to grant or withhold the remedy. We therefore agree with Toulson J in *Fyffes* that the ordering of an account in a non-fiduciary case is not automatic. One ground on which the court may withhold the remedy is that an account of profits would be disproportionate in relation to the particular form and extent of wrongdoing: see *Satnam* at 672b-c; *Walsh v Shanahan* [2013] EWCA Civ 411. In our judgment that is the case here."

Derivative claims

65. Put simply, a derivative claim is an exception to the general rule that the only legal person entitled to pursue a claim in respect of alleged wrongs done to a company is the company itself. Provided that certain conditions are satisfied, a shareholder may be entitled to pursue a claim by, in effect, standing in the shoes of the company.

66. Prior to the coming into force of the Act, the regime for derivative actions was governed by what is known as 'the rule in *Foss v Harbottle*'.[5] The effect of this rule was that minority shareholders could proceed with a derivative claim if, for example:

    66.1. The company was under the control of the wrongdoers, giving rise to a fraud being committed on the minority shareholders; or

    66.2. An *ultra vires* or illegal act had occurred which could not be ratified or confirmed by the company.

67. The codification of derivative action claims now appears in sections 260 – 264 of the Act. In broad terms, the position is as follows:

    67.1. Pursuant to section 260 (3) of the Act, a derivative claim under Chapter 1 of Part 11 of the Act "may be brought only in respect of a cause of action arising from an actual or proposed act or omission involving negligence, default,

[5] [1843] 67 ER 189

breach of duty or breach of trust by a director of the company." Plainly this includes breach of fiduciary duty on the part of an individual director(s).

67.2. An individual director(s) may therefore be the defendant to such a claim.

67.3. With regard to a shareholder's *locus standi* to bring a derivative claim, by section 260 (4) of the Act it is It is immaterial whether the cause of action arose before or after the person seeking to bring or continue the derivative claim became a member of the company.

67.4. There is no requirement to prove that the individual director(s) benefitted personally from the alleged wrongful conduct.

67.5. There is no requirement to prove that the individual director(s) who committed the wrongful act(s) control the majority of the company's shares;

67.6. There is no requirement for a shareholder to obtain permission prior to issuing a claim form for a derivative claim.

67.7. However, there is a two stage process for seeking the Court's permission to *continue* with a derivative claim. The applicable rules of procedure are contained within CPR, r. 19 and Practice Direction 19C. In summary:

67.7.1. At the first stage, the shareholder bringing the derivative claim must make a written application to the court, under CPR, r.23, for permission to continue the claim; in so doing, the shareholder must submit evidence which establishes a *prima facie* basis for pursuing the claim. Neither the company nor the individual defendant(s) is required to submit evidence at this stage of the proceedings. The court may dismiss the application on the papers. If it does so, the shareholder may request an oral hearing to reconsider the decision to dismiss the permission application.

67.7.2. If the claim is not dismissed at the first stage, the court may direct the company to provide evidence prior to a contested permission hearing. At that hearing, the court may dismiss the claim or grant permission to continue the claim (on whatever terms the court deems fit), and/or make other case management directions (including adjourning the hearing).

67.8. Section 263 of the Act stipulates a range of factors that the court must take into account, when considering an application for permission to continue a derivative claim.

67.9. If certain conditions are satisfied, leave *must* be refused. Specifically, section 262 (2) of the Act stipulates that leave must be refused if the court is satisfied:

> "(a) that a person acting in accordance with section 172 (duty to promote the success of the company) would not seek to continue the claim, or
>
> (b) where the cause of action arises from an act or omission that is yet to occur, that the act or omission has been authorised by the company, or
>
> (c) where the cause of action arises from an act or omission that has already occurred, that the act or omission—
>
> > (i) was authorised by the company before it occurred, or
> >
> > (ii) has been ratified by the company since it occurred."

67.10. Otherwise, the court has a discretion whether or not to grant leave, taking into account the range of factors laid down in section 263 (3) of the Act, namely:

> "(a) whether the member is acting in good faith in seeking to continue the claim;
>
> (b) the importance that a person acting in accordance with section 172 (duty to promote the success of the company) would attach to continuing it;
>
> (c) where the cause of action results from an act or omission that is yet to occur, whether the act or omission could be, and in the circumstances would be likely to be—
>
> > (i) authorised by the company before it occurs, or
> >
> > (ii) ratified by the company after it occurs;
>
> (d) where the cause of action arises from an act or omission that has already occurred, whether the act or omission could be, and in the circumstances would be likely to be, ratified by the company;
>
> (e) whether the company has decided not to pursue the claim;

(f) whether the act or omission in respect of which the claim is brought gives rise to a cause of action that the member could pursue in his own right rather than on behalf of the company."

67.11. Section 260 (4) of the Act further provides that: "In considering whether to give permission (or leave) the court shall have particular regard to any evidence before it as to the views of members of the company who have no personal interest, direct or indirect, in the matter."

<u>Green Paper proposals on strengthening stakeholder voices on company boards</u>

68. The Government's Green Paper on 'Corporate Governance Reform' was issued on 29 November 2016 and the consultation period ended on 17 February 2017.

69. Pages 34 – 42 of the Green Paper address the topic of 'Strengthening the employee, customer and wider stakeholder voice.' Four principal options for reform in this area are discussed in the Green Paper, namely:

69.1. Creating 'stakeholder advisory panels';

69.2. Designating existing non-executive directors to ensure that the voices of key interested groups, especially that of employees, is being heard at board level;

69.3. Appointing individual stakeholder representatives to company boards; and

69.4. Strengthening reporting requirements related to stakeholder engagement.

70. Paragraph 2.29 of the Green Paper makes it abundantly clear that the Government is "not proposing to mandate the direct appointment of employees or other interested parties to company boards" – a topic that has generated considerable political debate. Perhaps unsurprisingly, the tone of the discussion does not give much encouragement to those who would like to see the imposition of new *legal* obligations, as distinct from "expectations" and/or an "industry-led, voluntary approach", in respect of 'employee engagement' issues.

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