

AN EXAMINATION OF THE DIRECTOR'S DUTY OF CARE AND SKILL UNDER COMPANY LAWS OF NIGERIA AND THE UNITED KINGDOM*

1.1 Introduction

In the case of a sole proprietorship, the sole proprietor personally takes charge of the affairs of his venture. In fact, *he* is his venture. However, for the registered company, having a distinct personality and, often, many shareholders, it becomes necessary to put a few persons in charge of matters for the whole. These few at the helm of affairs are the *directors*. Company legislations and the courts have created certain principles regarding the person and office of the company director. One of such principles requires the director to exercise care, skill and diligence in the course of discharging his duties. This is because the company is a mere legal fiction¹ and therefore, the directors are its directing mind and will and control what it does.² The company director is accordingly considered an agent of the company when he acts on its behalf and within his powers.³ He is obliged to observe care and skill as a “duty” because the company can enforce this against him in an action for negligence.⁴

The legal principle that requires the director to exercise care and skill, though now codified, was originally a common law creation developed from the tort of negligence. The director's duty of care and skill is simply a manifestation of the general duty of care imposed on all individuals in the conduct of activities, so that a person may be liable to pay compensation when found to have been negligent by causing harm to someone else.⁵ It is this same principle that is extended to corporate law. The duty stems from the idea of company law having to balance the need for directorial accountability with the need to permit a certain amount of entrepreneurial risk taking.⁶

* Hannatu Adamu, LL.B., B.L., Lecturer, Department of Commercial Law, Faculty of Law, A.B.U. Zaria. mamahannatu@yahoo.com; mamahannatu@gmail.com; 08036497147.

¹ *Ladejobi vs. Odutola Holdings Ltd* (2002) 3 NWLR (Pt.753) 121 C.A., at 153.

² *Bolton (Engineering) Co. Ltd. vs. Graham & Sons* (1957) 1 Q.B. 159.

³ See s.283(2) Companies and Allied Matters Act 1990 “CAMA” Cap C20 Laws of the Federation of Nigeria, 2004.

⁴ See s.279(3) and (9) and s.282(2) CAMA and ss.170(1), 174 and 178 UK Companies Act 2006 “CA”.

⁵ Worthington, S. (2001). *Reforming Directors' Duties*, London School of Economics (LSE) Research Online, pp.9-10. Retrieved October 25, 2013 from <http://eprints.lse.ac.uk/200/1/FinalMLRDDuties.pdf>.

⁶ Roach, L. (1999). The Director's Duty of Skill and Care: Has the Law Commission Got it Right? *Business Law Review*, 20(51): p. 4. Retrieved December 11, 2013, from http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1754664. Indeed, some have gone as far as to say that “companies are in business to take risk.” See Davies, L.P. and Worthington, S. (2012). *Op.cit.* at p. 522 and Worthington, S., *op.cit.*, p. 10.

Thus, on the one hand, the law ought to demand a certain amount of responsibility on the part of directors and on the other, creativity and initiative must not be stifled for they are the pillars of business ventures, which companies most often are. Still, risk taking by company management must be restricted to acceptable levels.

This duty essentially borders on the manner in which a director is required to act in discharging his obligations in the office he occupies. Literally, "care" means attention shown in order to avoid damage or error.⁷ "Skill" refers to know-how; an ability to do something well, especially because one has learned and practised it.⁸ A third though less prominent aspect of the duty, is "diligence" which connotes "working hard" while being "careful and thorough."⁹ It is also considered to be a term which equates to conscientiousness and attentiveness.¹⁰ Apparently, "diligence" carries a meaning similar to a combination of "care" and "skill" and is used for emphasis. This may explain the reason why some commentators and even judges neglect it altogether in interpretation. In relation to directors' duties, all three concepts are more often called "the duty of care and skill" as in the CAMA or simply "the duty of care," although *care*, *skill* and *diligence* each has its notional meaning.¹¹

Generally, the law does not demand of a director to hold any special skills or qualifications in order to be appointed to office. However, it has been held that since the director controls the company, the conferment of such powers on him entitles shareholders and stakeholders of the company to the best of services.¹² The duty applies to everything that directors do. The minimum degree of care, skill and diligence required, therefore, is what the law has been hard put to decide, over time. At first, the duty was judged by subjective standards and many court decisions in the late nineteenth and early twentieth century continuously endorsed this notion. Throughout the evolution of this principle from its common law origin, to its codification today, the standard has changed with time. However, the relatively recent codification of the duties of directors under the UK Companies Act 2006

⁷ Encarta Dictionaries (2009). Microsoft Encarta Premium DVD.

⁸ Longman Dictionary of Contemporary English. (2005). 4th edition, Pearson Education Limited, England, p. 1547.

⁹ Ibid. at 436.

¹⁰ Davies, J. A Guide to Directors' Responsibilities Under the Companies Act 2006. Certified Accountants Educational Trust, (2007), p. 38. Retrieved from <http://www.accaglobal.com/content/dam/acca/global/PDF-technical/business-law/tech-tp-cdd.pdf>, accessed March 27, 2013.

¹¹ Corkery, F.J. (1987). *Directors' Powers and Duties*. Longman Cheshire, Melbourne Australia, p. 131.

¹² See *Delta Steel Nigeria Ltd. vs. American Computer Tech Inc.* (1999) 4 NWLR pt. 597.

“CA” codified a change in the attitude of the courts towards the director’s duty of care and skill from the earlier common law position. The Companies and Allied Matters Act 1990 “CAMA” has a statement on this duty which has not changed since the enactment of the law over twenty years ago.

In view of the fact that the UK law is the more recent of the two, and the CAMA is overdue for review, this work considers the question whether or not the duty as codified under the CAMA, needs to be reconsidered. To achieve this, the article examines the evolution of the duty under consideration and its current codification under the CAMA and the CA in order to conclude on the codification more appropriate for modern business practice.

1.2 The Duty of Care and Skill under Early Common Law

The recognition of the duty of care and skill required of the company director started with the English courts before legislation. In imposing this duty, the most critical issue often considered by the courts was the question of the standard of care to be expected as well as the level of personal attention required of the director. Romer J. deliberated on these points while deciding **Re City Equitable Fire Insurance Co.**,¹³ which decision was considered the authority on the point for a long time at common law. In that case, the chairman of an insurance company committed frauds by purporting to buy treasury bonds just before the end of the accounting period and selling them just after the audit. By this method, a debt due to the company from a firm in which the chairman had an interest was considerably reduced on the balance sheet by increasing the gilt-edged securities shown as assets and the auditors could not detect this. It appeared that the directors of the company had left the management of its affairs almost entirely to the chairman and it was perhaps because of this that he had more easily been able to perpetuate his frauds.

After some very careful deliberations, Romer J. reached the following conclusion:¹⁴ namely that (i) the skill to be expected was merely what a person of the director’s knowledge and experience could reasonably be expected to display; (ii) a director was not bound to give continuous attention to the affairs of the company; and (iii) a director could trust others entrusted with specific duties to perform them honestly in the absence of grounds for suspicion.

Romer’s decision above substantially mirrored a much earlier

¹³ (1925) Ch. 407.

¹⁴ Ibid., at p. 428.

position held by Bacon VC in **Re Montrotier Asphalte Co (Perry's case)**.¹⁵ Many other decisions on the same point reached in cases reported in the late nineteenth and early twentieth centuries also took similar positions. In **Re Cardiff Savings Bank (Marquis of Bute's Case)**,¹⁶ for example, the English court had held a director not liable for certain irregularities in the lending operations of a bank, despite having attended a company meeting only once in 38 years.¹⁷ Apparently, he was only appointed to lend the company the prestige that came with his family's title and no more. In the words of Jessel MR, "neglect or omission to attend meetings is not the same thing as neglect or omission of a duty which ought to be performed at those meetings."¹⁸ Thus, it is better to stay away from meetings than to attend and be inattentive.¹⁹ Following this, the court also decided, in the case of **Re Brazilian Rubber Plantation and Estates**,²⁰ that a director may undertake the management of a rubber company in complete ignorance of everything connected with rubber, without accruing responsibility for the mistakes which may result from such ignorance, for "he is not bound to bring any special qualifications to his office."²¹

The common law propositions above clearly set more of a subjective, than objective, standard for the director in discharging his duties. In effect, the courts were saying that "the director is obliged only to do as much as could be expected from someone as incompetent and foolish as he happens to be."²² It has been opined that the courts' summations may have had non-executive, rather than executive, directors in mind, possibly because of the then popular belief that the non-executive director had no serious role to play within the company but was simply "a piece of window-dressing aimed at promoting the company's image."²³ Perhaps, Parliament and the courts did not want to discourage entrepreneurial activity by restricting access to the

¹⁵ (1876) 34 LT 716.

¹⁶ (1892) Ch. 100.

¹⁷ A similar decision was reached in the case of *Re Denham* (1883) 25 Ch. D. 752, where a director attended no meetings in a four-year period and therefore, was held not liable regarding a fraud that had occurred.

¹⁸ *Re Cardiff Supra*, at p. 109.

¹⁹ Corkery, F.J. op.cit., p. 136. Consider also the dictum of Lord Hatherley in *Land Credit Co. of Ireland vs. Fermanby* (1870) LR 5 Ch. App. 763 at 770-771, that "it is their (directors') duty to be awake (during meetings) and their being asleep would not exempt them from the consequences of not attending to the business of the company."

²⁰ (1911) 1 Ch. 425.

²¹ Per Neville, J. *ibid*.

²² Mackenzie. (1982). A Company Director's Obligations of Care and Skill. *Journal of Business Law*, 460 at p. 461. Cited in Finch, V. (1992). Company Directors: Who Cares About Skill and Care? *The Modern Law Review*, 55(2): 179-214, at p. 200.

²³ Davies, L.P and Worthington, S. (2012). *Gower & Davies: Principles of Modern Company Law*. 9th edition, Sweet and Maxwell, London, p. 518.

company format. Given the wide range of backgrounds from which directors could legitimately come, it would have been unrealistic to expect the conduct of all directors to be judged by a single benchmark.²⁴ In any case, several scholars have since criticized the laxity in standards proposed by the decisions, particularly the fact of their being unsuitable for modern time²⁵ and being unduly generous to the incompetent director.²⁶ In calling for higher standards, Gower argued, “as the business world comes to expect higher standards, the law should develop in step. What has handicapped legal development so far has been the failure of the courts to recognise that ‘directing is becoming a profession with developing standards of expertise.’”²⁷ Thus, having minimal or no knowledge in connection with the line of business of a particular company can no longer be tolerated of directors.

Criticism of the aforementioned decisions as well as a change in perception of company management²⁸ in time combined to change the attitude of the courts. Beginning from the decision in **Dorchester Finance Co. Ltd v. Stebbing**,²⁹ the common law standard for directors began to change. In that case, the plaintiff, which was a money lending company, had three directors, S, P and H. S was involved in the affairs of the company on a full-time basis, while P and H made only rare visits. S and P were qualified accountants and H, though in fact unqualified, also had considerable accountancy experience. At S’s request, P and H signed blank cheques in the company’s name which, unknown to them, enabled S to make unsecured loans to other persons and companies with whom he had some connection. Eventually, the loans could not be recovered by the company, which then brought an action against the three directors for alleged negligence and misappropriation of company’s property.

Foster J. held all three liable, especially S who was said to have been grossly negligent. P and H were also held to have failed to exhibit the necessary skill and care in their duties even as non-executive directors. Apparently, it made no difference that the evidence showed that they had

²⁴ Corkery, F.J. op.cit., p. 142 and Davies, J. op.cit., pp.39-40.

²⁵ See Ogbuanya, N.C.S. (2010). *Essentials of Corporate Law Practice in Nigeria*. Novena Publishers Ltd., Lagos, p. 345; Gower, L.C.B. (1961). *Final Report of the Commission of Enquiry on the Company Law of Ghana*, p. 146; and Worthington, S. op.cit. at pp.9-10.

²⁶ Finch, V. op.cit. at p.179

²⁷ Gower, L.C.B. (1961). In: *The Report of the Commission of Enquiry on the Company Law of Ghana*.

²⁸ Mainly arising from indications of a new statutory interest in responsible management and by developments at European Community level, in North America and in the Commonwealth.

²⁹ Though decided in 1977, reported much later: (1989) BCLC 498.

acted throughout in good faith. While their accountancy experience and qualification may have prompted the court to reach this conclusion,³⁰ the judge stressed the fact that as far as directors duties were concerned, there was no distinction to be drawn between executive and non-executive directors. It can therefore not be said with certainty that the court would not have come to the same conclusion had the directors not been so qualified.

This was certainly a marked departure from the earlier cases of the late nineteenth century. Unlike the decision of Neville J.³¹ that one could take up the directorship of a rubber company in complete ignorance of anything connected to rubber without accruing responsibility for any mistakes resulting from such ignorance, the English court in **Re Barings Plc. (No. 5)**,³² ruled that “directors have, both collectively and individually, a continuing duty to acquire and maintain a sufficient knowledge and understanding of the company’s business to enable them properly to discharge their duties as directors.” Clearly, the courts were beginning to have a rethink of their past decisions.

Another case which at once showed a marked departure from the earlier common law position and set the format for the present standard under the CA, is **Norman v. Theodore Goddard**³³ which was followed by **Re D’Jan of London Ltd.**,³⁴ all decided by the same judge, who held similarly in both cases that s. 214(4) of the Insolvency Act 1986 in relation to wrongful trading, properly expressed the standard to be expected of directors in the discharge of their duties. The said s. 214 applies where a company has gone into insolvent liquidation and, at some time before the commencement of the winding up, a director knew or ought to have concluded that there was no reasonable prospect of avoiding insolvent liquidation. If the director does not convince the court that he took every step he ought to have taken to minimise the potential loss to creditors, personal contribution to the company’s assets may be ordered. Section 214(4) judges the steps to be taken or conclusions to be reached by both objective and subjective criteria. The director’s actions or conclusions are judged by those of a reasonably diligent person who has both the general knowledge, skill and experience reasonably expected of a person carrying out the same functions as that director *and* the general knowledge,

³⁰ Wild, C. and Weinstein, S. (2009). *Smith & Keenan’s Company Law*. 14th edition, Pearson Education Limited, England, p. 339; Finch V. Op.cit. p. 201.

³¹ *Re Brazilian Rubber Plantation and Estates* (1911) 1 Ch. 425.

³² (2000) 1 BCLC 523.

³³ (1991) BCLC 1028.

³⁴ (1993) BCC 646.

skill and experience that that director actually has. As will be shown later in this work, this initiative taken by the courts subsequently received the backing of legislation so that the honest incompetent director and the unjustified optimist may now have something to fear under s.174 CA.

1.3 The Duty of Care and Skill under Nigerian Company Law

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

In order to further emphasise the duty in subsection (1), subsection (2) warns that “failure to take reasonable care in accordance with the provisions of section 282 of this Act shall ground an action for negligence and breach of duty.” To ensure that the director gives adequate care and attention to his duty to the company, and in order to deliberately deviate from the English court’s ruling in **Re City Equitable Fire Insurance Co.** above, s. 282(3) provides that “each director shall be individually responsible for the actions of the board in which he participated, and the absence from the board’s deliberation, unless justified, shall not relieve a director of such responsibility.”

Evidently, contrary to the position held by Orojo,³⁶ the position in Nigeria today is not the same as the common law at the time of the ruling by Romer J. The drafters of the CAMA deviated from the common law position noted by deliberately setting clear, objective standards in the sections

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

³⁶ Orojo, J.O. (2008). *Company Law and Practice in Nigeria*. 5th edition, LexisNexis Butterworths, Durban, South Africa, p. 269.

mentioned above, perhaps due to the obvious inadequacies observed in the subjective standard.

Essentially, the CAMA differs from the propositions proffered in the English cases in three ways. Firstly, by requiring the director to measure up to the standard of any "reasonably prudent director", the law thereby subjects him to an objective, reasonable man test. Thus, if a company appoints a moron, it is well within its rights to still expect him to measure up to the standard of a notional, reasonable director. It has been suggested³⁷ that the standard now seems to be set somewhere "between the level of the ignoramus or moron at one extreme and that of a top flight professional director at the other extreme." The provision therefore has the potential of encouraging any prospective director to decline a position he knows he is incompetent to fill.

Conversely, this also implies that, should any particular director in fact possess more skills or qualification than reasonably to be expected of the reasonable man or average director in his circumstance, he would still only be held accountable by the reasonable man's standard and the company cannot expect more from him, unless his service contract states otherwise. This may have the undesirable effect of not encouraging directors to acquire further skills or qualification or even neglecting to put them to use, where they possess them. Although s. 282(4) leaves no doubt that the same standard of care is required of both executive and non executive directors, a proviso further allows any service contract with the company to demand a higher standard or place additional liability in the case of the executive or service director.

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

³⁷ Osunbor, O.A. (1992). *The Company Director: His Appointment, Powers and Duties*. In: Akanki, E.O. (ed) *Essays on Company Law*, p 130, at 147.

be tried under the CAMA today, the Marquis would likely be found liable in negligence or breach of duty³⁸ having attended a company meeting only once in 38 years.

Thirdly, by cautioning the director against delegating his powers in a manner that may amount to an *abdication of duty*, s. 279(7) thereby encourages the director to be mindful of his obligations to the company, even where he delegates another to do the work. Granted, requiring the director to display reasonable care and skill implies that he himself is involved in the act of discharging his duty. Yet, it is conceded that due to some circumstantial exigency and the nature of the services directors provide for the company, it may be necessary for directors to delegate some tasks or responsibilities to other persons and indeed, the terms of their appointment may allow them to do so. On the other hand, the law realises the need to curtail unrestrained or excessive delegation of duties on the part of directors in order to curtail the abuse of the discretion given.

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

The case of **Adebayo vs. Johnson**,³⁹ though a misfeasance proceedings brought under s. 211 of the Companies Decree 1968, decided on the director’s duty of care and skill. Coker J.S.C. then set the record straight on the issue of delegation, observing that although the director is entitled to assume that qualified staff are performing their duties with competence, the chairman of the board and the managing director, by virtue of the nature of their offices, are expected to know better than others. The Supreme Court had no difficulty holding the directors in this case liable for deficiency after they were put on notice of irregularities regarding the company’s finances, yet still did nothing.

Though the decision above was decided based on the Companies Decree of 1968, the principle observed is no different from that in the present

³⁸ Refer to s. 282(2) CAMA.

³⁹ (1969) All NLR, 171.

CAMA. Although the court admitted the director's right to delegate as was observed in *Re City*, yet the court was quick to caution that he must not thereby *abdicate* his responsibility. Particularly, the decision recognised the special offices of the chairman of the board and the managing director as having the potential of being judged by higher standards of care and skill. Importantly, the court found their conduct as amounting to "gross negligence" in this case, suggesting that if their conduct had amounted to "mere negligence," they might have escaped liability.⁴⁰

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

More decisions from Nigerian courts would have been very useful in discerning exactly how much the CAMA has achieved in deviating from the early common law position. Regrettably, this writer has not been able to find any more directly on the director's duty of care and skill under the present law. It is debatable if there is.

The departure by the CAMA from the earlier common law position was an attempt to introduce professionalism in the office of the company director in accordance with modern day expectations. It is true that the company director is more in the limelight today than he was decades ago. Corporate failures around the globe involving Enron, WorldCom, Vivendi, Madoff, Parmalat, Cadbury and several Nigerian banks,⁴¹ have ensured that managers of companies are more in the spotlight now more than ever

⁴⁰ Apparently at common law, directors must be 'culpably' or 'grossly' negligent before they can be said to be in breach of the duty of care and diligence. See dicta of Romer J, Lindley MR and Rigby LJ respectively in *Lagunas Nitrate Co. vs. Lagunas Nitrate Syndicate Ltd.* (1899) 2 Ch. 392 at 418, 435 and 466 (CA). While the courts have long been unsure about exactly what 'gross negligence' means, apparently something more than what we may call 'ordinary negligence' is required. See Corkery, F.J. op.cit., p. 132.

⁴¹ Mostly due to inadequate supervision and weak management. See Nworji, D.I., Adebayo, O. and David, O.A. (2011). Corporate Governance and Bank Failure in Nigeria: Issues, Challenges and Opportunities. *Research Journal of Finance and Accounting*, 2(2): 3-4. Retrieved December 3, 2013, from www.iiste.org/Journals/index.php/RJFA/article/download/183/67.

before. The failures have been partly attributed to the appointment by companies of unqualified or unskilled directors as well as the latter's outright negligence of duty. Consequently, the practise in some jurisdictions today, such as the UK,⁴² Australia,⁴³ Hong Kong⁴⁴ and South Africa,⁴⁵ is for an added subjective standard required of directors. This is suggested as having the potential to augment the objective test in order to hold directors responsible where they have special skills or qualifications not necessarily possessed by their peers, whether they happen to be executive or non-executive directors.

Granted, the CAMA improved upon the former common law by requiring a uniform objective standard. But the practice these days judging from English legislation and decisions,⁴⁶ is to move beyond that to demand more from directors. This is because, in the past, directors didn't usually have any qualifications per se. Cases like **Re Brazillian** and **Re City** above clearly show that they were either put there in spite of their lack of knowledge and experience or simply because of the prestige that comes with their name. But in modern times, directors are more often educated and hold portfolios that testify to several qualifications, with impressive resumes. Even non-executive directors, who are in office simply to check management, are known to have their own qualifications. They are no longer expected to be mere figure heads, as corporate codes increasingly show.⁴⁷ Added to this, the office of company director these days is often specialized or departmentalised, so that a uniform standard would be either unduly unfair or even too generous. Thus, the practice these days is to require directors to live up to their resumes, that is, deliver as much as they hold out in capabilities, apart from the general rule of living up to objective standards. This is considered a better way by addressing the issue of standard of care in relation to specializations and company types. Thus, even a non-executive director, if he has any special qualifications or experience, will be bound to put it to the use of the company. Currently under s.282, the director need not display more than the reasonable standard, unless his service contract requires it. But

⁴² See s. 174 CA.

⁴³ See s.180(1) Australia Corporations Act 2001 (as amended).

⁴⁴ See s. 465 of the new Hong Kong Companies Ordinance 2012.

⁴⁵ See s. 76(3)(c) of the South African Companies Act 2008.

⁴⁶ See *Norman vs. Theodore Goddard* (1991) BCLC 1028; *Re D'Jan of London Ltd.* (1993) BCC 646 whose decisions informed s.174 of the UK Companies Act 2006. See also *Abbey Forwarding Ltd. (In Liquidation) vs. Hone* (2010) EWHC 2029 (Ch).

⁴⁷ See generally Nigeria Securities and Exchange Commission's Code of Corporate Governance for Public Companies 2011 and the Central Bank of Nigeria Code of Corporate Governance for Banks Post Consolidation 2006.

the law should apply the subjective test to a director with more experience than "reasonable" in addition to the minimum objective standard. This will be fairer to categories of directors and also discourage embellishment of resumes.

1.4 The Duty of Care and Skill under UK Company Law

Apparently, the drafters of the CA considered the courts' decisions in **Norman v. Theodore Goddard**⁴⁸ and **Re D'Jan of London Ltd.**,⁴⁹ to have been properly reached, so that "it is now accepted that the duty of care...is accurately stated in Section 214(4) of the Insolvency Act 1986,"⁵⁰ and confirmed in s. 174 CA thus:

- (1) A director of a company must exercise reasonable care, skill and diligence.*
- (2) This means the care, skill and diligence that would be exercised by a reasonably diligent person with—*
 - (a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company, and*
 - (b) the general knowledge, skill and experience that the director has.*

Evidently, as the High Court rightly observed in **Gregson vs. HAE Trustee Ltd and Others**,⁵¹ s.174 CA simply codified existing dicta from the previous case law discussed above. The law has thereby effectively classified directors so that s.174(2)(a) takes into consideration the particular responsibilities attached to the office of any particular director—for example, a director of sales in a computer software company. It is by the general standard of this class of directors that he is to be judged, so that the director's conduct should be appropriate for the particular position that he occupies. Further, if he happens to have special qualifications beyond those required under the general standards, s.174(2)(b) holds him to those extra qualifications—for example, if the director of sales happens also to be a

⁴⁸ (1991) BCLC 1028.

⁴⁹ (1993) BCC 646.

⁵⁰ Per Lord Goldsmith of the Lords Grand Committee at the Committee hearing on 6 February, 2006. See *Companies Act 2006: Duties of Company Directors* (2007). Ministerial Statements published by the Department of Trade and Industry (DTI), p. 12. Retrieved October 13, 2013 from <http://www.berr.gov.uk/files/file40139.pdf>.

⁵¹ (2008) EWHC 1006.

computer programmer. It is therefore, a cumulative requirement.⁵² In effect, a director having a lot of knowledge and experience would be expected to use it. Apparently, the difference between s. 174 and the earlier common law decisions is that in the latter, the director's subjective level of skill sets the standard required of the director, whereas under s. 174, the director's subjective level does so only if it improves upon the objective standard of the reasonable director.⁵³

The Act clearly does not distinguish between executive and non-executive directors with regard to the duties here discussed. However, although subject to a uniform and objective duty of care, what the discharge of that duty requires in particular situations will not necessarily be uniform for executives and non-executives alike, nor, for that matter, between different types of executive directors or even different types and sizes of companies.⁵⁴ This fact is evident from s.174 in stating that what the law would expect from the director would all depend on "the functions carried out by the director in relation to the company." Therefore, objective/subjective standard is also significant for non-executive directors because they would first be subjected to the standards of non-executives generally and then, if they happen to have any special knowledge or skills, to those subjective criteria. Thus, even non-executive directors may be subjected to higher standards than some executive directors, if the former happen to have some special qualifications.

A recent case which considered s. 174 is **Abbey Forwarding Limited (in liquidation) vs. Hone**,⁵⁵ wherein the English High Court observed that in deciding whether directors have fallen short of their duty of skill and care, particularly where the breach of duty concerned the precise way in which the business was run, evidence of what was normal in the field of commerce in which the company operates is of considerable relevance. The court then ruled that, taking various factors together, and in the absence of evidence about industry practice, it was not prepared to find the directors were in breach of their duty of skill and care to the company. Clearly, therefore, every case will be decided based on the relevant circumstances.

⁵² Per Lord Goldsmith of the Lords Grand Committee at the Committee hearing on 6 February, 2006. See *Companies Act 2006: Duties of Company Directors*. Op.cit. p.12.

⁵³ Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 520.

⁵⁴ Ibid.

⁵⁵ (2010) EWHC 2029 (Ch). cited in Bills Committee on Companies Bill: Follow-up to the Meetings on 3 and 10 June 2011 Supplementary Information (June 22, 2011). Financial Services and the treasury Bureau, Companies Registry, p. 8. Retrieved December 11, 2013, from <http://www.legco.gov.hk/yr10-11/english/bc/bc03/papers/bc030628cb1-2577-1-e.pdf>.

Of course "reasonable" is a highly nebulous term. It still remains to be seen how the courts would actually interpret "reasonably diligent person" as well as the things that may "reasonably be expected of persons" carrying out the functions of a director in relation to this duty. It is important for the courts to clearly interpret these terms because the benchmark which s. 174 attempts to set, is actually implicit in them.⁵⁶ Importantly, the imposition of an objective standard does not necessarily require a directorship to be regarded as a profession, since the courts would presumably define "what is reasonable" in relation to the director having regard to the knowledge, skill and experience which a person in his position ought to have.⁵⁷ Even non-executives would be required to measure up to some reasonable standard in carrying out their duties of guiding and monitoring the management of the company. A caution has been sounded, though, that the courts cannot afford to be too hard on directors in their interpretation of reasonableness, considering the complexities of modern companies where many transactions are carried out simultaneously in dispersed geographical locations, or they would make it difficult for boards to find directors.⁵⁸ Besides, the courts would not want to end up being made into assessors of business risk, a role for which they are obviously unsuited.⁵⁹

Interestingly, the demand for higher standards for directors in the discharge of their duties, resulted in the current practice whereby directors obtain insurance against their potential liability for negligence.⁶⁰ Indeed, s. 233 CA allows a company to purchase and maintain insurance for its director against liability arising from negligence and others. It is generally conceded that companies essentially take risks and so even where directors act in good faith while displaying the relevant care and skill, the result may still be disastrous. Thus, the fact that a company makes a loss, or even fails totally, is not necessarily indicative that its directors have been negligent in the management of the company's affairs.⁶¹ And since the law does not allow the company to relieve the director from the duty under s. 174,⁶² it is

⁵⁶ Davies, J. (2007). Op.cit., at p.42.

⁵⁷ Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 520.

⁵⁸ Pettet, B. (2010). *Common Law Duties of Care and Skill*. Retrieved December 11, 2013, from <http://law.oxj.co/common-law-duties-of-care-and-skill-93650/>.

⁵⁹ Davies, L.P. and Worthington, S. (2012). Op.cit. at p. 523.

⁶⁰ Pettet, B. Op.cit.

⁶¹ Worthington, S. op.cit. at p. 10.

⁶² Although curiously, s. 1157 empowers the court to excuse directors for breach of duties committed under reasonable circumstances. Hoffmann LJ. Rightly expressed doubts, in *Re D'Jan of London Ltd* (1994) 1 BCLC 561 that a person found to have been guilty of negligence, which involves failing to take reasonable care, can ever satisfy a court that he acted reasonably. It means that conduct may be "reasonable" for the purposes of s.1157 despite

submitted that in allowing the company to take out an insurance policy for its director, the law has thereby aided it in circumventing the law by insuring the director against whatever amount he may be asked to pay. Supposedly, the idea is that, in this manner, companies shield directors who make loss-generating decisions reasonably after collecting all the appropriate evidence and after appropriate consultation and evaluation. But it is argued, and this writer quite agrees, that fully insured directors may have little financial interest in taking care, particularly if they do not pay their own premiums.⁶³

In some jurisdictions,⁶⁴ this issue is effectively taken care of by the business judgment rule which is designed to accommodate such careful, yet unlucky directors. It has been suggested that there is no need for the equivalent of the business judgment rule in the CA, as the normal rules of negligence already accommodate instances covered by that rule.⁶⁵ Besides, even the business judgement rule is a protection available only to competent directors.⁶⁶ Usually, where a director is able to prove circumstances exonerating him from liability, he would not be found liable.

It is pertinent to note that although s. 174 clearly refutes some of the conclusions reached by Romer J. above, the part as to delegation, to a certain extent, remains an extant principle of UK corporate law.⁶⁷ In other words, the permission to delegate is still available to the director, although he must monitor the delegate reasonably to ensure the proper discharge of the responsibilities. In *Re Barings Plc.*,⁶⁸ the court clarified that the fact that a director is allowed to delegate “does not absolve a director from the duty to supervise the discharge of the delegated functions.”⁶⁹ However, when once the director discharges this duty to the best of his ability, while being confident of the person he has put in charge, he cannot be liable for the negligence or fraud of that delegate or employee. In any case, his liability would all depend on the circumstances.⁷⁰

The duty under s. 174 is particularly important because of the

amounting to lack of reasonable care at common law.

⁶³ Finch, V. op.cit. at p. 212.

⁶⁴ Notably, the United States of America and Australia.

⁶⁵ Law Commission and Scottish Law Commission. *Company Directors: Regulating Conflicts of Interest and Formulating a Statement of Duties*, Cm. 4436, 1999, Pt. 5; Worthington, S. op.cit, p. 10.

⁶⁶ Finch, V. op.cit. at p. 189.

⁶⁷ Especially considering s. 170(3) and (4) acknowledges the continued application of common law principles presumably not in conflict with the Act.

⁶⁸ (No. 5) (2000) 1 B.C.L.C. 433.

⁶⁹ Per Jonathan Parker J. *ibid.* at p. 489.

⁷⁰ See *Lexi Holdings Plc vs. Luqman* (2009) EWCA Civ 117.

Company Directors Disqualification Act 1986 and the Insolvency Act 2000, which combine to generally disqualify certain persons in certain situations from being involved in the formation or management of companies and, in particular, from being company directors in the future.⁷¹ Any director found liable for the breach of the duty under s. 174 can, as a result, be disqualified for a period ranging from 2 to 15 years, from holding directorship positions.⁷² This is apart from the publication of his name in a register maintained by the Secretary of State, which effectively puts him on a notional “red list” so that companies and the public may take note.

It has been opined that the view that more qualified persons are subjected to higher standards of duty, is counter-productive in the long term, as it may deter such able, qualified persons from opting for the office.⁷³ It is here submitted that this may not be the case. Such directors can effectively retaliate by raising their “prices” or contract with the company to take out insurance policies on their behalf. Conversely, directors owe it to their company—indeed, it is in harmony with the expectation of good faith on their part—to afford the company any and all special qualifications they have, especially if this was the basis upon which the company hired them in the first place. Obviously, the new regime proposed by the tenor of s. 174 requires prospective directors to be alert to their future responsibilities. A director cannot complain that the standards required of him by s. 174 are unfair. He does have a choice whether or not to accept directorial responsibility, after considering his qualifications and the level of commitment he knows he is prepared to put in. The English court has observed, rightly in this writer’s view, that

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

⁷¹ See ss. 6 and 11 of the Company Directors Disqualification Act 1986.

⁷² Such a disqualification order was made in relation to some senior executive directors following the collapse of Barings Bank. See *Baker vs. Secretary of State for Trade and Industry* (2001) BCC 273.

⁷³ Roach, L. op.cit., at p. 3. According to this author, “it is surely a better state of affairs to attract qualified, educated professionals and risk a minority of them not bringing their expertise to bear, than to deter such people to such an extent that our boardrooms are devoid of solicitors, accountants and other professionals.” A similar worry was expressed by Lockhart J. in *Australian Innovation Ltd. vs. Paul Andre Petrovsky* (1996) 14 ACLC 1357.

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

1.5 Conclusion

The standard described under s.282 CAMA greatly improves from that required under the earlier common law. But it can be better. It is certainly not the best suited for today's business climate whereby directing comes with varieties of companies and positions within companies. Furthermore, directors today, whether executive or non executive, present impressive resumes to their companies. Although the standard set by s.282 CAMA would require the incompetent director to perform up to the level of a notional director in the same situation, the provision has the potential to allow a director who is actually more competent than the notional director, to escape liability, unless there is a service contract between him and the company which requires him to exercise higher standards of skill and care. Non- executive directors do not usually have service contracts. The dual objective/subjective liability threshold provided under s.174 CA and many other company laws of other jurisdictions, apart from considering 'reasonability' based on function and company type, has the further advantage of taking such situations into consideration, and is therefore, the more suited to the realities of the office of company director today.

In view of the fact that society expects much more from the director today and also in view of the fact that directors today more often have several qualifications, the company should be entitled to expect more from the person who presents himself as skilful in a particular field, even without a service contract with the company. Thus, any director, where he happens to be knowledgeable or skilful in a particular area, should be held to those standards as a default rule, even in the absence of a service contract. Therefore, s.282 CAMA should be amended to reflect the model in s.174 by which directors are held to a dual objective/subjective standard. In addition, the publication of the names of directors disqualified for negligence, should be considered. This will encourage better appointments and prospective directors would pay more attention to their capabilities and responsibilities

⁷⁴ Re Barings Plc. (No. 5) (2000) 1 B.C.L.C. 523.

more seriously. In the long run, companies and investors will benefit from better corporate governance.