DIRECTORS' DUTIES IN THE MODERN WORLD

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A roadmap

- Setting the scene: interplay between common law duties and statutory regulation.

- The Senior Managers' Regime – claims against directors for regulatory non-compliance.

- A footnote on CDDA 1986 'compensation orders'.

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Common law duties & statutory regulation

- Directors have traditionally owed the company a duty of skill and care at common law (albeit the standard was low: *Cardiff Savings Bank. Marquis of Bute's case* [1892] 2 Ch. 100)

- Common law duty of care now codified in s.174 of the Companies Act 2006 (& see s.170(4).

- Hoffmann LJ in *Re D'Jan of London Ltd* [1993] BCC 646 – dual standard: objective / subjective.

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Common law duties & statutory regulation

- Factors which affect the extent of the duty:

  - Experience of the director & his role / part in the company;

  - Structure of the Company / manner in which the business is organised;

  - Level of reward paid to the director: “the higher the level of reward, the greater the responsibilities” (*In Re Barings plc* (No 5) [1999] 1 BCLC 433;

  - The terms of any service agreement with the Company;

  - The type of business of the company & the role of statutory regulations to which the company is subject (e.g. environmental / financial / import *Re Centrix Commercicals* (unreported)).

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The Senior Manager’s Regime

- From March 2016, the “Senior Managers and Certification Regime” replaced the “Approved persons Regime” for banking and insurance firms.

- It applies to the most senior individuals in a relevant business that perform a “key role”.

- Its aims are increasing governance standards, raising individual accountability, and restoring confidence in the sector.

- Ongoing Financial Conduct Authority (“**FCA**”) consultation (26 July 2017 – 3 November 2017) in relation to extending the regime to all regulated firms.

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Senior Manager’s Regime

- The SMR requires that authorised firms map responsibilities and identify the individuals responsible for key areas of governance, compliance and operations to increase individual accountability.

- Individuals at all levels can be held to appropriate standards of conduct.

- Senior managers can now be held accountable for misconduct falling within their area of responsibility.

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Claims against directors for regulatory non compliance

The FCA may take action against a person for misconduct if:

- it appears to the FCA that the person is guilty of misconduct; and
- the FCA is satisfied that in all the circumstances it is appropriate to take action against the person.

(Section 66, Financial Services & Markets Act 2000 (the "**FSMA**")).

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Claims against directors for regulatory non compliance

- The limitation period within which the FCA must commence proceedings is six years, beginning with the first day on which the FCA knew of the misconduct, (s.66(4) FSMA).

- The FCA is to be treated as knowing of misconduct if it has information from which the misconduct can reasonably be inferred, (s.66(5)(a) FSMA).

- Proceedings are treated as begun when the FCA gives the person a warning notice under s.67(1) FSMA.

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Claims against directors for regulatory non compliance

If the FCA is entitled to take action against a person then the enforcement tools include:

- imposing a penalty in an amount the FCA considers appropriate;
- suspending, for such period as the FCA considers appropriate, any approval of the performance by the person of any function to which the approval relates;
- imposing, for such period as the FCA considers appropriate, any conditions in relation to any such approval which it considers appropriate;
- limiting the period for which any such approval is to have effect;
- publishing a statement of the relevant misconduct.

(S.66(3) FSMA).

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The test for taking action against a person under s.66 FSMA is a two stage test:

- it must appear to the FCA that the person is guilty of misconduct; <u>and</u>
- the FCA must be satisfied that it is appropriate in all the circumstances to take action.
- S.66A FSMA contains provisions about when a person is guilty of misconduct for regulatory enforcement purposes.

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Claims against directors for regulatory non compliance

- It is important to draw the distinction between enforcement against a person for misconduct under s.66 FSMA and enforcement against a senior manager for misconduct.

- An authorised person, or a director or employee of an authorised person, or an approved person of the authorised person can be guilty of misconduct where the criteria set out at s.66A(2) and/or (3) FSMA are met.

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Claims against directors for regulatory non compliance

A director or employee can be guilty of misconduct where:

- the director or employee has failed to comply with applicable rules of conduct made by the FCA; and/or

- the director or employee has at any time been ‘knowingly concerned’ in a contravention of a relevant requirement imposed on an authorised person pursuant to the FSMA.

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Claims against directors for regulatory non compliance

By contrast, a senior manager can be guilty of misconduct and thus exposed to regulatory sanction if:

- the manager has at any time been a senior manager in relation to an authorised person;
- at the time, there has been or is continuing a contravention of a relevant requirement by the authorised person;

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- the senior manager was at that time responsible for the management of any of the authorised person's activities in relation to which the contravention occurred; and

- the senior manager did not take such steps as a person in the senior manager's position could reasonably be expected to take to avoid the contravention occurring (or continuing).

(S.66A(5) FSMA).

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Claims against directors for regulatory non compliance

- The FCA will need to determine that the senior manager was responsible for management of the activities in relation to which the relevant breach took place.
- The FCA will consider the ‘full circumstances’ of the case and will look at, amongst other things:
    - the firm’s management responsibilities map;

Claims against directors for regulatory non compliance

- the senior manager’s actual role and responsibilities in firm, to be determined by reference to, among other things, minutes of meetings, emails, regulatory interviews, telephone recordings and organisational charts; and

- how the firm operated and how responsibilities were allocated in practice.

(See Decision, Procedure and Penalties Manual (DEPP) within FCA Handbook at DEPP 6.2.9C).

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- The FCA will need to determine whether the senior manager failed to take such steps as a person in the senior manager's position could reasonably be expected to take to prevent the relevant contravention.

- Those steps are such steps as a competent senior manager would have taken:

  - at that time;
  - in that specific individual’s position;
  - with that individual’s role and responsibilities; and
  - in all the circumstances.

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There are eighteen separate factors listed at DEPP 6.2.9-E including:

- whether the manager exercised reasonable care when considering the information available to them;
- whether the manager reached a reasonable conclusion on which to act;
- the nature, scale and complexity of the firm's business;
- the knowledge the senior manager had, or should have had, of regulatory concerns, if any, relating to their role and responsibilities.

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- The FCA will bring enforcement action against individuals as well as firms.
- The FCA stresses the importance of co-operation with the FCA.
- The use of enforcement tools is ‘less likely’ where the relevant firm has developed an open and communicative relationship with the FCA and can demonstrate to the FCA that senior management takes its responsibilities seriously.

(See Enforcement Guide (EG) within the FCA Handbook at EG 2.11.1 and 2.12.2).

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- Contravention by an authorised person of a rule made by the FCA is actionable at the suit of a private person who suffers loss as a result of the contravention, subject to the defences and other incidents applying to actions for breach of statutory duty, (s.138D(2) FSMA).

- Breach of the Senior Manager’s Regime and conduct rules are not actionable under s.138D FSMA.

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Compensation Order (CDDA 1986)

- s. 110 of the Small Business, Enterprise and Employment Act 2015 introduced a new ‘compensation order’ regime into the CDDA 1986.

- Conditions are (i) a disqualification order has been made (ii) director’s conduct caused loss to a creditor(s)

- Time Limit: 2 years from disqualification order/ undertaking.

- Amount of the order depends on (i) amount of loss, (ii) conduct of director and (iii) whether any financial recompense has been made.

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