

Directors' duties to disclose conflicts of interest: *Fairford Water Ski Club v Cohoon & Craig Cohoon Watersports* [2021] EWCA Civ 143

On 9 February 2021, the [Court of Appeal](#) unanimously allowed Mr Cohoon and Craig Cohoon Watersports' ('**Watersports**') appeal against the decision of His Honour Judge Russen QC at first instance ([\[2020\] EWHC 290 \(Comm\)](#)).

The Court of Appeal's judgment in *Fairford v Cohoon* provides helpful guidance on the operation of section 317 of the Companies Act 1985 ('**CA 1985**') as well as its successor, section 177 of the Companies Act 2006 ('**CA 2006**'). The case will be of interest to practitioners who advise directors on the duties they owe to a company.

Background to the appeal

Fairford Water Ski Club ('**the Club**') is a company which runs a members' club for water skiing and associated activities. The Club is the freehold owner of a lake and surrounding land in Fairford, Gloucestershire. The Club's Articles of Association incorporated regulation 84(1) of Part 1 of Table A in Schedule 1 to the Companies Act 1948 ('**CA 1948**'), which in turn incorporated section 199 of the CA 1948. By 2007, section 199 of the CA 1948 had been replaced by section 317 of the CA 1985¹.

Mr Cohoon was the chairman and a director of the Club until January 2017. He was also a partner of Watersports, an unincorporated partnership whose business involved running a water ski school and selling water ski equipment. Mr Cohoon ran Watersports from a building which was leased from the company and for which Watersports paid an annual rent of £20,000.

In 2007, the Club entered into a management agreement with Watersports, whereby the Club paid to Watersports the annual sum of £35,000 for managing the lake and surrounding land. The agreement was terminated in January 2017, when new directors were appointed and Mr Cohoon resigned.

In October 2017, the Club commenced proceedings against Mr Cohoon, Watersports and Mr Cohoon's wife and son for a number of alleged breaches of their duties when they were directors of the Club. While some 38 claims of varying degrees of significance were advanced at first instance, one successful claim – which was the subject matter of Mr Cohoon's appeal before the Court of Appeal - concerned the repayment of sums paid out under the management agreement for the period 2007 to 2017. At first instance, HHJ Russen QC found that Mr Cohoon failed to declare the nature of his interest in Watersports at a board meeting prior to the management agreement coming into effect, as required by section 317 of the CA 1985.

The consequence of the judge's finding was that the Club was entitled to recover management fees paid during the six years prior to the issue of the proceedings. The Claimant's contention that section 21(1)(b) of the Limitation Act 1980 ('**LA 1980**') applied so as to enable it to recover management fees paid out before 2011 was rejected.

¹ Section 177 of the Companies Act 2006 came into force on 1 October 2008: see the Companies Act 2006 (Commencement No. 5, Transitional Provisions and Savings) Order (S.I. 2007/3495). Section 317 of the CA 1985 continues to apply in relation to a duty before arising before that date.

Issues on appeal

Mr Cohoon and Watersports appealed against HHJ Russen QC's decision that the fees paid out to Watersports in respect of the Management Agreement should be recovered by the Club. The Club also cross-appealed against the finding that it was not entitled to recover sums pre-dating 2011.

The Court of Appeal was asked to consider a number of issues on the Defendants' appeal and the Claimant's cross-appeal². In respect of the appeal, such issues included the proper interpretation of section 317 of the CA 1985, the juridical basis for the judge's remedy where there has been an alleged breach of the no conflict rule, the availability of *restitutio in integrum*, and the reach of section 1157 of the CA 2006. At the centre of the Claimant's cross-appeal was the question whether an award for breach of section 317 of the CA 1985 constituted the recovery by the Claimant of proceeds of trust property for the purposes of section 21(1)(b) of the LA 1980.

The Court's findings on liability

The Court of Appeal reversed HHJ Russen QC's decision on appeal, and held that the nature of Mr Cohoon's interest in Watersports had been sufficiently disclosed to the Club's directors at a board meeting in January 2007. Many of the issues raised on the appeal therefore fell away so as not to be considered by the Court, as did the Claimant's cross-appeal.

The Court's findings on liability turned on its interpretation of the language and purpose of section 317 of the CA 1985. In this respect, the Court identified six relevant principles:

1. Section 317 of the CA 1985 is cast in wide terms, and the nature of the declaration which the director has to make in order to comply with their duty will depend on the nature of their interest and context in which the conflict arises³.
2. The director must declare their interest at a board meeting and must make the declaration, even if the interest is known to the other directors⁴.
3. The disclosure should be made before the contract is concluded, and the reference to a '*proposed contract*' contemplates that the terms of the contract may not necessarily have been finalised⁵.
4. The declaration must be made at the time when the question of entering into the proposed contract is '*first taken into consideration*'. If the contract is being considered by the directors over a series of board meetings, the declaration must be made at the first meeting, but need not be repeated subsequently⁶.
5. Section 317(1) of the CA1985 refers to a specific notice of a conflict in a proposed contract, and this subsection must be read compatibly with the general notice provisions in sections

² *Fairford Water Ski Club v Cohoon & Craig Cohoon Watersports* [2021] EWCA Civ 143 ('*Fairford v Cohoon (CA)*'), at [39] to [51] and [58].

³ *Fairford v Cohoon (CA)*, at [43] to [45].

⁴ *Ibid.*, at [46]. Note that section 177(2) of the CA 2006 does not require a declaration to be made at a board meeting: '*177(2) the declaration may (but need not be) made (a) at a meeting of the directors or (b) by notice to the directors in accordance with (i) section 184 (notice in writing), or (ii) section 185 (general notice).*'

⁵ *Ibid.*, at [47].

⁶ *Ibid.*, at [48].

317(3) and 185 of the CA 1985⁷. A director's declaration need not be extensive if they are to satisfy the requirements of a general notice; they comply with their duty once they declare that they are a member of a specified company and are to be regarded as interested in any future contract which may be made with that company.

6. The purpose of section 317 of the CA 1985 is to ensure directors disclose their interests in a proposed contract. The court should not imbue this section with any additional requirement to ensure that directors act in good faith or put the interests of the company's members first⁸.

What does the judgment in *Fairford v Cohoon* mean for directors?

Although the Court of Appeal's judgment focuses on the proper interpretation of section 317 CA 1985, directors and their legal advisers can gain a valuable insight into the courts' treatment of section 177 of the CA 2006.

Nature of the disclosure: The Court drew an interesting distinction between uncomplicated contracts involving the company and director, and contractual arrangements where a director's interest is not so clear and obvious. In the latter case, a fuller explanation of the nature of the director's interest might be necessary if one is to satisfy the requirements of section 317 CA 1985⁹.

The language of section 177 of the CA 2006 differs from section 317 of the CA 1985: in the former, the director must declare the '*nature and extent*' of their interest, yet the latter provision refers to a declaration of the '*nature*' of the director's interest. A submission was made that the two provisions should be interpreted differently in light of this difference. While that point fell away during the course of submissions, Males LJ seemed to suggest the two terms are, in any event, synonymous with one another¹⁰. The distinction drawn by the Court in respect of different types of contract therefore remains relevant in cases of alleged breaches of section 177 of the CA 2006.

Timing for making the disclosure: contracts will often be contemplated by directors over a number of board meetings. The wording '*at the meeting of the directors at which the question of entering into the contract is first taken into consideration*' does not appear in section 177 of the CA 2006. There is no strict rule under section 177 of the CA 2006 to make the required declaration at a board meeting of directors. Rather, it states only that '*any declaration required by this section must be made before the company enters into the transaction or arrangement*'¹¹.

However, some similarity in language can nonetheless be drawn from both provisions on this timings issue. In a case under section 317 CA of the 1985, the duty is engaged in respect of a '*proposed contract*', while in a case alleging a breach of section 177 of the CA 2006 case, the director must disclose their interest in a '*proposed transaction or arrangement*'. As stated above, the final terms need not have been settled when the director discloses their interest in the contract being contemplated. The

⁷ *Ibid.*, at [49].

⁸ *Ibid.*, at [50].

⁹ *Ibid.*, at [45].

¹⁰ *Ibid.*, at [53].

¹¹ Companies Act 2006, Section 177(4).

criticism levelled at Mr Cohoon in this litigation was that his declaration was made at a time when the specific fee to be paid under the management agreement was not wholly settled¹².

Relief from liability: although this case did not turn on the question of relief from liability, the Court made the interesting remark that, had Mr Cohoon breached his duty to disclose under section 317 of the CA 1985, the breach was of a highly technical nature. Equally, the Court observed the oddity of any potential finding of liability since a director in Mr Cohoon's position would not have breached his duty had such a contract been proposed only one year later, after 1 October 2008. By this time, section 177(4) of the CA 2006 was in force, which provides that a director need not declare an interest if, *inter alia*, the other directors are, or ought reasonably to be, already aware of it¹³.

Conclusion

Fairford v Cohoon remains relevant to practitioners advising directors on breaches of the no conflict rule which post-date 1 October 2008. The Court of Appeal's judgment provides useful guidance on the question of liability, and the central question is whether the other directors were '*fully informed of the real state of things*'¹⁴ at a point before the contract was finalised.

Hugh Sims QC and Katie Gibb acted for Mr Cohoon and Watersports at first instance and on the appeal. Hugh and Katie were instructed by Harrison Clark Rickerbys.

Case note drafted with the assistance of Charlotte Mallin-Martin, pupil.

¹² *Fairford Water Ski Club v Cohoon & Ors* [2020] EWHC 290 (HC), at [80] and [235] to [240].

¹³ Companies Act 2006, Section 177(6)(b).

¹⁴ *Gray v New Augarita Porcupine Mines Ltd* [1952] 3 DLR 1 (PC), at [14], as cited in *Fairford v Cohoon* (CA), at [44].