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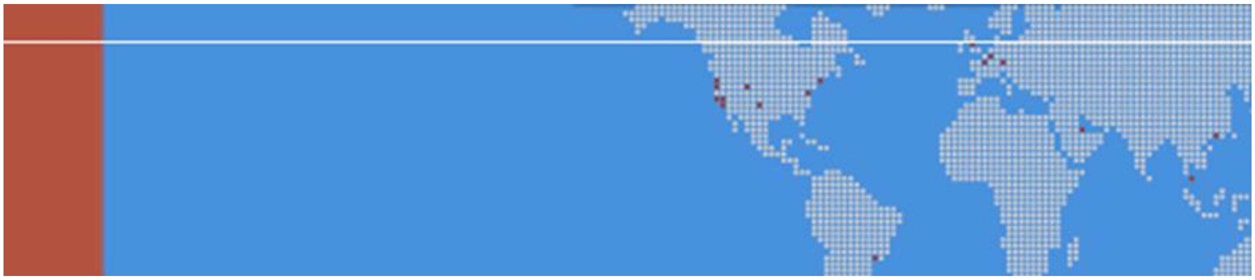

UK Client Guide

Duties of Directors of UK Subsidiary Companies – An Introduction

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INTRODUCTION

Directors of unlisted private companies incorporated in the UK

This guide gives an overview of the duties of directors of unlisted private companies incorporated in the UK. While these duties will often coincide with the strategy and requirements of the subsidiary's parent company, it is not always the case and the circumstances may require a director to act independently of the parent.

It should be noted that a person who assumes the role of a director (for example by attending and voting at board meetings) may be considered to be director for these purposes, even if not formally appointed as such. A person may also be considered to be a "shadow director", and therefore subject to the same duties, if the other members of the board of the company are accustomed to conduct its business in accordance with that person's instructions.

Personal Liabilities

Directors also risk personal liability and this is increasingly so as regulators are taking tougher stances especially toward bribery, corruption and anti-competitive behavior, particularly cartel abuses. Directors and prospective directors will therefore want to know the extent to which they can protect themselves against these risks.

The regulatory framework that Directors need to be aware of is broad and this introductory guide brings together the principal elements under relevant statutes and regulations, as well as the common law, and sets out the potential liabilities and the practical steps that can be taken to avoid them.

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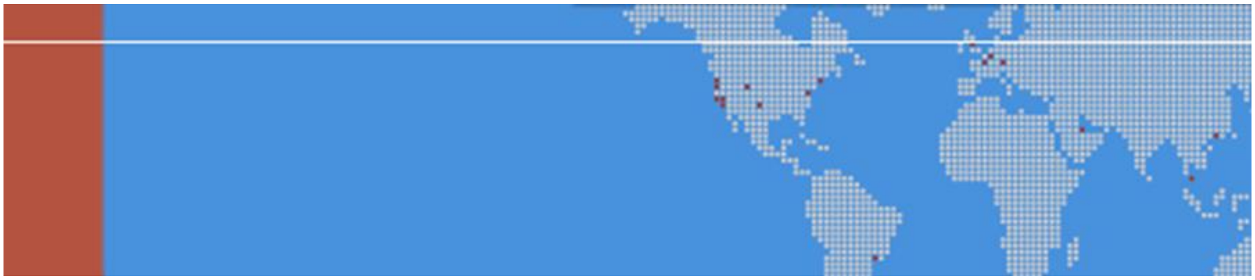


GENERAL CORPORATE DUTIES

Where do these duties come from, and to whom do I owe them?

General duties originally came from common law and were derived from case law developed over many years. They have since been codified by the Companies Act 2006, but the courts must still refer to common law when interpreting them.

Duties may also arise under the constitutional documents of your company, such as the memorandum and articles of association, and you must ensure you are familiar with the documents as a director of the company.

You owe the duties to your company, not to other group companies (including the parent), individual shareholders or groups of shareholders.

What are my general duties?

There are seven general duties. You must:

Act within your powers

This means exercising your powers in accordance with the company's constitution and for the purposes for which they were conferred. For example, you should not exercise your powers so as to benefit the interests of a parent company over the interests of the company.

Promote the success of the company

You have a duty to act in a manner you consider, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole. In deciding to promote the success of the company, you are required to have regard, among other matters, to:

- the likely long-term consequences of your decisions;
- the interests of the company's employees;
- the need to foster the company's business relationships with suppliers, customers and others;
- the impact of the company's operations on the community and environment;

- the desirability of maintaining a reputation for high standards of business conduct; and
- the need to act fairly as between members of the company.

Although all the listed factors must be considered, in many cases the board may be able to conclude quickly that a particular factor is not relevant.

The Companies Act 2006 does not expressly require the board minutes to record that the factors were considered, although some companies may decide they want to include a reference to having considered the factors as evidence that they did this.

Exercise independent judgement

You can, of course, continue to rely on the judgement of others in areas that you are not expert, if you exercise your own judgement in deciding whether to follow particular advice or to accept someone else's. You can also delegate matters to committees on the same basis.

Exercise reasonable care, skill and diligence

You must act as a reasonably diligent person. This person is taken to have the general knowledge, skill and experience that may reasonably be expected of a person carrying out the same functions as you, and your general knowledge, skill and experience. The first requirement is an objective test; the second looks to your particular knowledge, skill and experience.

Avoid conflicts of interest

In a case not involving a transaction or arrangement with the company (where an obligation to disclose arises, see below), you must avoid a situation in which you have, or could have, a direct or indirect interest or duty that conflicts or possibly may conflict with the company's interest. This is unless the board has already authorised the matter (see Conflicts below).

Not accept benefits from third parties

You must not accept a benefit from a third party, unless the benefit cannot reasonably be regarded as likely to cause a conflict of interest. Board guidance on the circumstances in which accepting benefits will not be reasonably regarded as likely to cause a conflict may be helpful, but will not be decisive.

Declare your interest

You are not under a duty to avoid interests in transactions or arrangements with the company, but you must disclose any interest in a transaction or arrangement that the company proposes to enter into, or that it has entered into, whether your interest is direct or indirect. The declaration must be made before the transaction or arrangement is entered into, or if in relation to an existing transaction or arrangement, as soon as reasonably practicable.

You may disclose an interest in a transaction or arrangement with the company to the other directors. You can do this at a board meeting, by written notice or by general notice. The notice must state that you are interested in a specified body corporate or firm or are connected with a specified person. You must declare the nature and extent of the interest, and you must provide updates should your previous declaration become inaccurate or incomplete, e.g. because your interest changes.

Do I have the same duties if I am a non-executive director?

A non-executive director's duties are no different from those of an executive director because the statutory statement of general duties applies to both.

In practice, executive directors will likely be subjected to higher standards of skill and care in the discharge of their duties because they are involved in the day-to-day management of the company. In addition, case law recognises that non-executive directors will rely on others to help them comply with their duties.

However, the extent to which executive directors and other professionals may reasonably be relied on to perform non-executive directors' duties depends on the circumstances. For example, a non-executive director with an accounting qualification would be expected to exercise more active scrutiny of the company's accounts than a director without an accounting qualification. Since non-executive directors have the same rights of access to information about the company as executive directors, they are expected to ask for appropriate information.

What are the consequences if I breach these duties?

You may:

- be personally liable to compensate the company for a loss caused as a result of a breach;
- have to restore company property; and

- have to account for profits made or received.

The company may have the right to rescind a contract that has been entered into where there is a conflict of interest.

The Companies Act 2006 also introduced a statutory right for shareholders to sue directors, in the company's name, to recover any loss the company has suffered as a result of the directors' negligence, default, breach of duty or breach of trust, if certain conditions are met. This is known as a 'derivative action.'

CONFLICTS

What are my duties relating to conflicts?

Under the Companies Act 2006, you have statutory duties relating to three areas of conflicts:

- situational conflicts – you must avoid situations where your interests conflict (or may possibly conflict) with the company's interests, or have them authorised by the board (e.g., you having a shareholding in a competitor);

- transactional conflicts – you must declare interests in transactions or arrangements with the company (e.g., if the company is deciding to enter into a contract with a supplier or supplier that you have an interest in); and

- accepting benefits – you must not accept benefits from third parties if it would reasonably be regarded as causing a conflict of interest (e.g., accepting a bribe or extravagant corporate hospitality).

In addition, your company's articles of association may also require you to take particular steps if a potential conflict of interest arises.

What types of conflict need to be authorised?

Actual and potential conflicts may require authorisation. Therefore, you will need authorisation if you:

- have multiple directorships – if you sit on more than one board, you are advised to have all your directorships authorised;

- are a shareholder in a competing company or a company that is an actual or potential customer of, or supplier to, your company;
- own a property next to your company's property or otherwise of value to your company that could affect, or be affected by, your company's activities;
- have an advisory relationship (e.g., financial, accountancy, legal or consultancy) with your company or have an interest in an advisory firm;
- are a trustee of your company's group pension scheme or a director of its trustee company;
- take up an opportunity that has been offered to the company even if the company has declined it or you are in a position to make a profit as a result of your directorship; or
- are offered a role by a potential bidder for the company.

These examples are not exhaustive. You should only use them as a prompt to consider the types of situations for which you may need authorisation. The safest approach is for all actual and potential conflicts to be authorised by the board if there is any doubt.

Are 'connected persons' relevant to my duties?

In some cases the interest or duty of someone who is connected with you may be treated as your indirect interest or as causing a conflict of interest or duty. This will be a question of fact. In some circumstances there may be scope for arguing that it is not your indirect interest, but in most cases it will be safer to assume that it may be.

The categories of connected person include:

- family members, including a spouse or civil partner, anyone with whom you live as a partner in 'an enduring family relationship', children and stepchildren (your own and your partner's) and your parents;
- bodies corporate that you are connected with (detailed rules determine when this will be the case);

- trustees of a trust that you (or a family member or a body corporate that you are connected with) are a beneficiary; and

- your business partner.

Must I be aware of conflicts?

There is no breach of your duties relating to conflicts if you are unaware of an interest or are unaware of the transaction or arrangement. But you are treated as aware of all matters that you ought reasonably to be aware of. This will depend on the facts.

How does authorisation work?

In deciding whether to authorise a potential conflict, the board should consider what should happen if a conflict actually arises. In particular, it should consider whether any conditions should be imposed by the terms of the authorisation – for example, that you should not attend board meetings at which any relevant matter is discussed. Even if an authorisation is unconditional, a conflict may make you uncomfortable in practice. If you are an executive director of one company and a non-executive of another, you may feel uneasy attending the meetings of both boards when something under discussion is relevant to both. The best course may be to absent yourself from both meetings and to arrange not to receive papers for the matter that you are interested in.

Board authorisation can be given only if:

- any quorum requirement is met without counting any interested director; and

- the matter is agreed without counting any interested director's vote.

What practical steps can I take?

When seeking authorisation, you should make the fullest possible disclosure of all matters likely to be relevant to avoid any suggestion that the authorisation given was not fully informed. You will need to update your details on an ongoing basis when you become aware of a new actual or potential conflict.

If a potential conflict arises, you should immediately notify your company.

You should also advise your company if you have any direct or indirect interests in existing or proposed transactions or arrangements with your company that have not already been disclosed to the board.

If a specific conflict arises, particularly in sensitive areas such as a possible bid, you should seek independent advice. If it is not possible to disclose the conflict and, if necessary, obtain authorisation, it may be necessary for you to absent yourself from relevant board discussions or even to resign.

THE UK BRIBERY ACT

The Bribery Act came into force on 1 July 2011. It repeals existing bribery offences and introduces new ones – including, for the first time, a corporate offence of failing to prevent bribery.

What constitutes an offence?

The Act creates four categories of offence, which address the following:

- offering, promising or giving a bribe to another person;
- requesting, agreeing to receive or accepting a bribe from another person;
- bribing a foreign public official; and
- a corporate offence of failing to prevent bribery.

The most significant departure from the previous law is the last offence, a new strict liability offence for companies of 'failing to prevent bribery'. A company will commit the offence if an associated person performing services on its behalf bribes another person to obtain or retain either business or a business advantage for the company. However, a company will have a complete defence if it can show that, at the time the offence was committed, it had in place adequate procedures to prevent bribery. HM Government has issued extensive guidance on the meaning of "adequate procedures".

Importantly, the corporate offence has extra-territorial application. It applies to any UK-incorporated company and any overseas entity that carries on a business or part of a business in the UK. Crucially, the associated person that carries out the act of bribery on behalf of the organisation does not need to have any connection with the UK.

What are the penalties?

The maximum penalty for the general offences of bribing another person and being bribed is 10 years' imprisonment. The penalty for the corporate offence is an unlimited fine. Directors convicted of a bribery offence may also be subject to disqualification, which could result in their disqualification from holding a director position for up to 15 years. Debarment from public contracts is also a potential consequence of Bribery Act violations by companies.

Am I responsible for others?

Directors of companies will also be concerned to know whether they may be in the firing line for the company's transgressions. The Bribery Act provides for a senior officer, which includes directors, to be liable if it can be shown that the company committed one of the Bribery Act's main offences with the officer's consent or connivance (which, according to the Government's guidance, includes "turning a blind eye")

In practice, prosecutors may find it difficult to convict senior officers owing to the initial requirement that the company must have committed one of the three main offences. The Bribery Act does not provide any new mechanism for corporate liability in relation to these offences and so the existing attribution test of 'directing the mind and will' would still need to be satisfied. Historically, prosecutors have struggled to convict organisations using this test. A senior officer cannot be liable for the corporate offence of failing to prevent bribery.

What practical steps can I take to avoid any offence being committed?

In terms of practical steps, there is no one-size-fits-all approach to responding to the Act (in particular as regards "adequate procedures"), but you and the company may want to consider:

- preparing and publishing a global code of conduct across all group companies, which is continually monitored and revised;

- setting up an internal anti-corruption committee with reporting responsibility to the board, tasked with assessing the company's bribery risk on an ongoing basis;

- strong communications and training (both internal and potentially also to key business partners) on anti-bribery and corruption that set the "tone from the top";

- clear policies on gifts, corporate hospitality and lobbying;

- robust screening processes for third party payments; and

- clear channels for staff to escalate concerns in confidence (such as an ‘ethics hotline’).

The overriding message from the Serious Fraud Office (SFO) and the government is that paper policies are insufficient. In particular, the SFO has made it clear that there is a focus on the role of individuals, and especially senior officers, who consent to or connive in bribery. It is expected that the SFO will use this focus in order to drive behavior and an ethical culture within companies. The SFO has made it clear that it expects senior officers to consider resigning and blowing the whistle if efforts to establish an ethical culture meet with resistance or no success. Expressing doubts but remaining in office, the SFO has said, may constitute conniving in bribery for the purposes of the legislation.

Accordingly, what matters is what is happening in practice within the organisation and whether there is a pervasive culture against corruption.

THE ENVIRONMENT, HEALTH AND SAFETY AND COMPETITION

What are my obligations concerning the environment?

The Companies Act 2006 now requires you, when complying with the duty to promote the success of the company, to consider the impact of the company’s operations on the community, its employees and the environment.

You should be aware of any environmental legislation that applies to the company’s business in all jurisdictions in which it operates. Shareholder activism, facilitated by the availability of the derivative action procedure, is often focused on the effect of companies on the environment and local communities.

Even companies operating outside industries associated with obvious environmental risks can be affected by environmental legislation – due, for example, to the presence of historical contamination that requires remediation or even to the amount of energy they use.

Committing pollution offences may cause criminal liability punishable by a fine or imprisonment or both, subject to the nature and gravity of the offence. Civil liability may also arise under common law, causing claims for damages or injunctive relief. In other European jurisdictions, environmental offences are normally dealt with through an administrative penalty, usually a fine. This system has also been introduced in the UK: the Environment Agency, the environmental regulator in England and Wales, has the power to impose civil sanctions on companies and individuals, such as fines of up to £250,000, for certain environmental offences.

Personal liability can be imposed on you for breaches of environmental law if, as a result of your acts or omissions, you create circumstances:

- that cause the commissioning of the offence;
- where the offence is proved to have been committed with your consent or connivance or neglect; or
- where the offence is attributable to your act or neglect.

If you are convicted of such an offence, you can be disqualified from being a director.

What are my obligations concerning health and safety?

The Health and Safety at Work etc Act 1974 takes a similar approach to the protection described above regarding environmental offences. You may be personally liable for health and safety offences where you can be said to have commissioned the offence or where the offence can be proved to have been committed with your consent, connivance or neglect.

The Health and Safety (Offences) Act 2008, which came into force in January 2009, means serious breaches of health and safety rules can attract a custodial sentence of up to two years. If you are convicted of such an offence, you can be disqualified from being a director.

As a result of high-profile cases, public attention has also focused on companies' and directors' criminal liabilities under the common law for gross negligence as a result of the death of employees or third parties. The Corporate Manslaughter and Corporate Homicide Act 2007 (the Corporate Manslaughter Act), which came into force in April 2008, introduced a statutory offence of corporate manslaughter in England, Wales and Northern Ireland, and corporate homicide in Scotland. It means companies and other organisations may now face criminal prosecutions for manslaughter.

The Corporate Manslaughter Act does not increase personal liability for individual directors or managers. Rather, it is directed at companies and other organisations against which verdicts of 'corporate killing' have in the past been difficult to secure. However, you can be prosecuted for gross negligence manslaughter where the prosecution can prove that:

- you owed a duty of care to the deceased;

- a breach of that duty has occurred; and
- the breach was so grossly negligent that you can be deemed to have had such disregard for the life of the deceased that your conduct should be seen as criminal.

In many cases where a death occurs in a work situation, prosecution under the Corporate Manslaughter Act, as well as for lesser offences under the Health and Safety at Work etc Act, is now likely to be considered and investigated by the enforcement and prosecution agencies. The Sentencing Guidelines Council published definitive sentencing guidelines in February 2010. The guidelines recommend a starting point of £500,000 for corporate manslaughter cases and £100,000 for deaths arising from health and safety law breaches, but with a clear indication the fine should be 'punitive and sufficient to have an impact on the defendant'.

In February 2011, Cotswold Geotechnical (Holdings) Ltd (Cotswold) became the first company to be charged with and convicted of the offence of corporate manslaughter under the Corporate Manslaughter Act. Initially, one of Cotswold's directors was also charged with gross negligence manslaughter. However, due to his ill health, these charges were stayed.

Cotswold was convicted against a background in which it had failed to take all reasonably practicable steps to protect an employee taking soil samples at the bottom of a 3.5 metre trial pit. The company ignored well-recognised industry guidance that prohibited entry into excavations more than 1.2 metres deep and, at the time of the employee's death, Cotswold had left him unsupervised on site.

What are my obligations concerning competition law?

The UK Enterprise Act 2002 contains provisions that impose personal liability on directors for breaches of competition rules by the companies they run.

The "cartel offence"

An individual is guilty of an offence (punishable by a prison term of up to five years and/or an unlimited fine) if he or she dishonestly agrees with others to fix prices, limit production or supply, divide customers or markets, or rig bids. The offence is committed whether or not the agreement is implemented.

Competition disqualification orders

You may be disqualified as a director (for up to 15 years) if your company commits a breach of European or UK competition law and the court considers your conduct makes you unfit to be concerned in the management of a company.

In deciding whether or not you are unfit, the court will consider whether:

- your conduct contributed to the breach of competition law;
- you had reasonable grounds to suspect a breach but took no steps to prevent it; or
- you did not know but ought to have known that there was a breach.

Factors which the court will take into account include whether a director made sure that his company took quick remedial steps (and implemented them properly) and whether any disciplinary action was taken against the responsible employees.

"Whistleblowing"

A company which is involved in a cartel can escape liability (both for itself and its employees) if it acts as a "whistleblower" and seeks immunity by reporting the cartel to the Office of Fair Trading. Directors should be alter to take advantage of this possibility as soon as information concerning a cartel comes to their attention, as immunity (as opposed to leniency) may not be available if another cartel participant blows the whistle first.

If you suspect your company may be involved in anti-competitive behaviour, you should immediately seek legal advice.

RESTRICTED TRANSACTIONS

Are there restrictions on particular transactions between the company and me?

Shareholder approval is required before you or persons connected with you (for a definition of connected person, see Conflicts) can acquire non-cash assets from the company or parent company where the value of the assets exceed £100,000 (or, if less, 10 per cent of the company's net asset value (however, amounts below £5,000 are disregarded). The same applies where your company or a subsidiary acquires non-cash assets from you or a person connected to you.

If shareholder approval is not obtained, you and all the directors who authorised the transaction are liable to account to the company for any profit and must indemnify the company against any loss or damage.

Can my company give me a loan?

The Companies Act 2006 contains complex rules requiring shareholder approval before the company or parent company can make or guarantee a loan to you. In the case of public companies and their subsidiaries, the need for shareholder approval extends to arrangements by which the company agrees to meet expenditure on your behalf (a ‘quasi-loan’) and to hire purchase-type arrangements that may benefit you. They also apply to loans, quasi-loans and credit transactions to those connected with you. There are exceptions to these restrictions, broadly relating to:

- the size of the loan (loans that do not exceed £10,000 can be made to you for any purpose);
- the purpose of the loan – subject to conditions (including obtaining shareholder approval) a greater sum is permitted if the loan is to meet expenditure incurred on behalf of the company or to enable you to perform your duties properly; and
- the nature of the company – a money-lending company has additional exemptions.

INSOLVENCY

What are my duties in an insolvency situation?

The Insolvency Act 1986 imposes duties and requirements on you that are designed to protect the interest of the company’s creditors if the company has become, or is likely to become, insolvent.

If the company’s financial position has deteriorated to the point where its solvency is in question, your attention must shift away from the shareholders and towards protecting the interests of creditors.

You must consider the interests of creditors as a whole, not just the interests of any creditor or class of creditor. You are subject to these duties even if appointed as a representative of a particular creditor.

What is ‘wrongful trading’?

Wrongful trading is trading without any reasonable prospect of avoiding a liquidation that leaves creditors unpaid. In these circumstances, there is potentially no value for shareholders left in the company and the directors owe their primary duties to creditors.

How can I incur liability for wrongful trading?

Liability arises if you conclude or should have concluded that insolvent liquidation is inevitable and you do not take every step to minimise potential loss to creditors. You will be deemed to be armed with a reasonable degree of competence to enable you to judge the company’s position. In addition, account will be taken of your experience. For example, if you are also a qualified accountant, you would be expected to understand financial information in a way that an unqualified director would not.

Only a liquidator can pursue a director for wrongful trading. No other party (such as a disgruntled creditor) has standing to sue. Liability generally equates to the loss caused to creditors as a result of the wrongful trading. Furthermore, a court must disqualify a director of an insolvent company if, in the court’s opinion, that person’s conduct as a director makes the individual unfit to undertake the management of a company.

When should my company stop trading?

Your company should stop trading once there is no reasonable prospect of avoiding insolvent liquidation. However, there may be a period when a company is facing difficulties but it is not yet certain that there is no reasonable prospect of avoiding insolvent liquidation.

In some cases, the loss to creditors can be minimised only by the company immediately filing for insolvency. This would be the case where the company considers itself unable to continue trading without the benefit of a formal insolvency process.

In other cases, however, ceasing to trade can be the very thing that might cause wrongful trading liability. This would apply where the loss to creditors can be minimised by the company continuing to trade because, for example, the company or the assets of the company can be sold and their value will be enhanced by the continuation of the company.

What practical steps can I take?

- Seek professional advice. The board should regularly seek appropriate legal and accountancy advice to ensure it is complying with its responsibilities.

- Board meetings should be held regularly and fully minuted. Regular meetings should show the directors' intention to consider all possibilities to minimise loss to creditors.

- Keep the decision whether to stop trading under review. If there is no hope of a successful restructuring/rescue, trading may have to stop immediately to avoid incurring liabilities that cannot be met. However, a premature decision to stop trading may be equally dangerous. For example, losses to creditors may be minimised by completing work in progress that would otherwise be valueless. Professional advice can be invaluable in helping directors make the right decisions and showing that they acted appropriately.

- Review transactions. When a company's solvency is in question, the review of any transaction that might be perceived as preferential or at an undervalue must be conducted with particular care. If you authorise a transaction that is subsequently reversed (because it is deemed preferential or at undervalue), you may be in breach of your duties to the company.

What if I sit on the board of two companies within the same group and one of those companies is in financial distress?

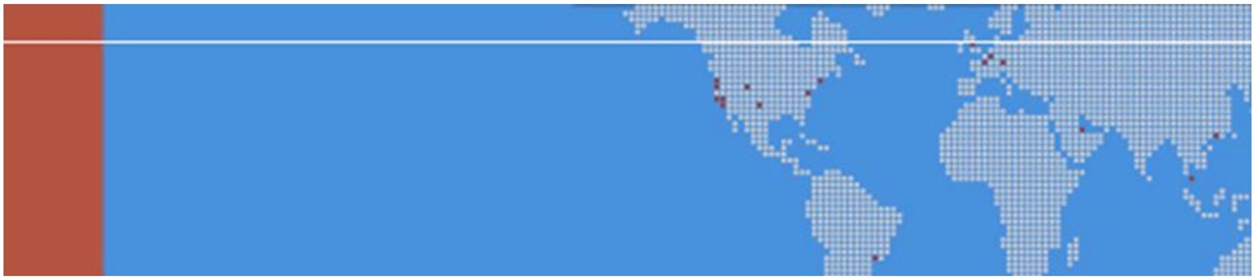
You may find yourself in the firing line if your company is in financial distress. In that case you must take extra care in discharging your duties. This can be made harder in a group if you are a director of several companies within a solvent group and one of those companies is insolvent. This may lead to a conflict of interest (see Conflicts).

If you find yourself with multiple directorships in a financially distressed group, you must consider how you make decisions. Importantly, you should take independent legal advice and monitor the decision-making process at every stage in light of that advice.

The following practical guidelines may be of use.

- Ensure there are several different directors on the board of each company to enable the appropriate procedures to be implemented.

- If a board is to discuss issues relevant to another group company that are not to be disclosed to that company, it should consider excluding from those discussions a director who is on the board of both companies, or the director in question should ask to be excluded. This should be recorded in the minutes so that there is a proper record should this ever become an issue.



- Frequently, decisions may have to be made concerning both companies. Therefore, it is useful to have specific provisions in each company's articles of association allowing for a reduced quorum on certain matters. This would enable the conflicted director not to attend while allowing the board meetings to be held with the reduced quorum.

- If this becomes unworkable, the director may consider resigning from one board. While this might increase the risk of wrongful trading, it may be the only option in extreme cases. This course should not be taken without specific independent legal advice and careful documentation of the decision.

- Both boards should check that they have adequate directors and officers insurance (see Indemnification, Insurance and Ratification).

INDEMNIFICATION, INSURANCE AND RATIFICATION

What do I need protection from?

You may be personally liable for your actions under a range of heads of liability, including:

- breaches of duties to the company (e.g., where a shareholder brings a derivative action in the company's name);

- breaches of duties to third parties (e.g., for a misleading statement in a prospectus for which the directors have taken responsibility);

- orders under statute (e.g., for wrongful trading under the Insolvency Act 1986);

- fines and restitution orders imposed by regulators and the courts; and

- legal and other costs incurred in defending proceedings.

The proper execution of your duties will go a long way towards mitigating liability, but you should ensure you are protected to the fullest extent in case of any claims.

Can the company indemnify me against liabilities?

A company may indemnify you against any liability for any negligence, default, breach of duty or breach of trust by you in relation to the company. However, this does not include liability incurred by you:

- to the company or to an associated UK company (which is, in effect, a company in the same group);
- to pay a criminal fine or regulatory penalty (a fine imposed by the Financial Services Authority (FSA), for example);
- in defending criminal proceedings in which you are convicted;
- in defending civil proceedings brought by the company or an associated company in which judgment is given against you; or
- in applying unsuccessfully for relief from liability under the Companies Act 2006.

How should the indemnity be given?

Since you may be unable to enforce an indemnity in your company's articles of association directly (because the articles do not necessarily constitute a contract between you and the company), it is safer to include appropriate wording (as far as permissible) in your contract of service or letter of appointment. Alternatively, the company may enter into a separate deed of indemnity with you.

Is insurance possible?

A company can insure you against most of your liabilities. Directors and officers insurance is designed to protect directors and officers of a company from a loss resulting from claims made against them regarding the discharge of their duties. However, insurance will not cover loss due to fraud or dishonesty, wilful default or criminal behaviour.

The FSA prohibits companies it regulates from entering into insurance contracts that would pay a financial penalty imposed by the FSA. The prohibition does not, however, affect the ability of FSA-regulated insurers to provide cover for the payment of compensation.

You can insure against some personal liabilities; for example, negligence, default, breach of duty and breach of trust in relation to the company. Insurance may also cover derivative claims brought by shareholders. Again, you cannot be insured for fraud or dishonesty, wilful default or criminal behaviour.

Can shareholders ratify a breach of duty by me?

Shareholders can ratify conduct by a director amounting to negligence, default, breach of duty or breach of trust by ordinary resolution (unless otherwise stated in the company's articles). The votes of the director (if the director is also a shareholder) and any connected persons are disregarded in such a resolution (for a definition of connected person, see Conflicts).

However, you should be aware that there are limits to what shareholders can ratify. For example, if a transaction entered into is illegal or constitutes a fraud on the company's creditors, shareholders cannot ratify it. In that situation, you risk being personally liable.

EUROPEAN GOVERNANCE GUIDANCE

EcoDa guidance and principles for unlisted companies in the Europe

In April 2010, the Institute of Directors published a European Confederation of Directors' Association (ecoDa) initiative titled Corporate Governance Guidance and Principles for Unlisted Companies in Europe (the ecoDa guidance). The ecoDa is 'the European voice of board directors', representing 55,000 board members across the EU. The ecoDa guidance is designed to provide guidance for European unlisted companies on the issues entailed in setting up a suitable corporate governance framework, noting that 'despite their large numbers and economic importance, the governance of unlisted companies is an often neglected area of corporate governance studies and recommendations'.

The ecoDa guidance:

- details the relevant actors and concepts that should be included in such a framework;
- highlights some of the challenges in implementing good corporate governance; and
- lists principles of good governance with key points and practical considerations. The ecoDa hopes these principles will provide a foundation for the development of country-specific principles in individual EU member states.

In November 2010 the European Confederation of Directors' Associations published corporate governance guidance and principles for unlisted companies in the UK. The guidance adapts, for the UK, ecoDa's guidance and principles for unlisted companies in Europe, for the UK and is substantially similar to the original European guidance. Amendments, made by the Institute of Directors, to the original guidance include the addition of descriptions and examples of UK company law and practice, and the removal of general descriptions of European law and practice.

FUTURE EUROPEAN GOVERNANCE DEVELOPMENTS

European Commission consultation on corporate governance

In April 2011, as part of a longer term review of the corporate governance framework of companies, the European Commission launched a consultation on a wide range of corporate governance issues, such as diversity in boards, shareholder engagement and the quality of corporate governance statements. The consultation paper aimed to launch a general debate on several issues.

Although the consultation focused on listed companies, the Commission noted that good corporate governance also matters to shareholders in unlisted companies, as company law provisions do not cover many relevant areas of corporate governance. There would not be a direct transposition of provisions applicable to listed companies to unlisted companies, as the challenges the two categories face are very different.

However, the consultation (which was open until July 2011) considered whether EU action is required on corporate governance in unlisted companies. In particular the Commission suggested the promotion of voluntary codes for non-listed companies. The Commission issued a feedback statement summarising the results of the consultation in November 2011. Around 70% of respondents thought that no EU action was required and that this issue should be left to the national level, particularly because of concerns related to increasing costs for unlisted companies. However, it is still for the Commission to determine whether legislative or non-legislative proposals are required. If such proposals are required they would be accompanied by a detailed impact assessment which will take account of the need to avoid undue administrative burdens.

Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding the above developments. Please contact the Gibson Dunn lawyer with whom you work, or Jeffery Roberts (+44 20 7071 4291, jroberts@gibsondunn.com), James Cox (+44 20 7071 4250, jcox@gibsondunn.com), Patrick Doris (+44 20 7071 4276, pdoris@gibsondunn.com) or James Ashe-Taylor (+44 20 7071 4221, jashetaylor@gibsondunn.com) in the firm's London office.

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