

KEY POINTS

- A common feature of syndicated loans is the role of Agent and the delegation by companies of functions in connection with the syndicated loans.
- In most cases delegation will be a lawful and commercially pragmatic act.
- But there are pitfalls for the unsuspecting director who remains personally responsible for discharging his director's duties to the company.
- Delegation should be thoroughly considered, suitably monitored and absent any actual conflict of interest.

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Delegation not abdication: directors' duties under scrutiny in syndicated loans

In syndicated lending it is common for lenders to delegate functions to an Agent and equally common for companies within a group to authorise the parent to act on their behalf. That has ramifications for the directors of the delegating companies – and for the directors of the delegate. This article considers the issues which may arise.

DELEGATION

The starting point is that directors are responsible for the management of the company's business for which purpose they may exercise all the powers of the company. This wording, or similar wording, appears in Model Articles prescribed by Sch 1 to the Companies (Model Articles) Regulations 2008 SI 2008/3229 (Sch 1) (and its predecessor Table A) and has been construed by the courts to confer decision-making powers on the board of directors acting collectively (*Mitchell and Hobbs (UK) Ltd v Mill* [1996] 2 BCLC 102).

However, delegation of board functions is a common occurrence and often a practical necessity for boards otherwise faced with company business of excessive complexity or volume. Despite its widespread incidence, such delegation is only permitted if, and to the extent that, the company's articles of association expressly permit the delegation. Any board resolution purporting to delegate authority to another contrary to the articles may be held to be ultra vires.

MODEL ARTICLES

The current model articles for companies contain provision for delegation. Thus, in the case of a company limited by shares, Art 5 to Sch 1 provides:

"5. Directors may delegate

- (1) Subject to the articles, the directors may delegate any of the powers which are conferred on them under the articles—
- (a) to such person or committee;

- (b) by such means (including by power of attorney);
 - (c) to such an extent;
 - (d) in relation to such matters or territories; and
 - (e) on such terms and conditions;
 - (f) as they think fit.
- (2) If the directors so specify, any such delegation may authorise further delegation of the directors' powers by any person to whom they are delegated.
- (3) The directors may revoke any delegation in whole or part, or alter its terms and conditions."

Similar provisions are also contained in reg 71 and 72 of Table A, the default articles of association under the Companies Act 1985.

DIRECTORS: A PERSONAL APPOINTMENT

Delegation would appear at first blush to run counter to the personal nature of a director's appointment. It is trite that a director is appointed personally and cannot delegate the discharge of his duties in that position to another. Similarly, he cannot absolve himself from personal responsibility by taking no active role in the company or failing to inform himself of company business.

In *Re Westmid Packing Services Ltd (No 3)* [1998] BCC 836, a company disqualification case, Lord Woolf MR, giving the judgment of the Court of Appeal, emphasised at p 842:

"... that the collegiate or collective responsibility of the board of directors of

a company is of fundamental importance to corporate governance under English company law. That collegiate or collective responsibility must however be based on individual responsibility. Each individual director owes duties to the company to inform himself about its affairs and to join with his co-directors in supervising and controlling them.

A proper degree of delegation and division of responsibility is of course permissible, and often necessary, but not total abrogation of responsibility."

Similarly, it is not a defence to a breach of duty claim pursuant to s 1157 of the Companies Act 2006 to rely on inactivity as such conduct is "by definition unreasonable" (*Lexi Holdings plc v Luqman* [2007] EWHC 2652 (Ch)).

DIRECTORS' DUTIES

The consequence of the above is that, even where delegation is permissible pursuant to the articles and a commercial imperative, individual directors must remain cognisant of their duties in respect of acts carried out by the delegate.

The core duties of directors are set out in ss 171-177 of the Companies Act 2006. Those duties include a duty to:

- act in accordance with the company's constitution and only exercise powers for the purposes for which they are conferred (s 171);
- act in the way he considers, in good faith, would be most likely to promote the success of the company (s 172);
- exercise independent judgment (s 173);
- exercise reasonable care, skill and diligence (s 174); and
- avoid a situation in which he has, or can have, a direct or indirect interest that

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conflicts, or possibly may conflict, with the interests of the company (s 175).

Assuming that the articles permit the delegation, it is unlikely that a director will be in breach of s 171 as a result of the board's delegation of functions.

However, even if the act of delegation itself is in conformity with a director's duties, it is clear from the caselaw discussed above that a director is not entitled to sit back and expect a delegate to perform his director's duties for him. He remains personally accountable as director.

DIRECTORS' DUTIES IN A GROUP STRUCTURE

In practice delegation within a group structure and between connected companies can often raise acute issues of conflict of interest for a director. Taking a simple scenario, it is not uncommon for a director of a parent to also be a director of a subsidiary, and for some purposes the parent may be the delegate for the subsidiary. The resulting overlap in personnel is often a matter of commercial pragmatism and ensures a vital information flow within the business. Directors of a company delegating to such a common director or the common director himself must have particular regard to whether the arrangements conform to their duties to the companies of which they are director.

In cases where a director of a subsidiary has regard to the interests of the group, the following principles are well-established:

- That a director must not be guided by the interests of the group as a whole if this might be detrimental to the interests of his own company, particularly if the company has separate creditors.
- However, if the intended measure does not conflict with the interests of his company, it is not a breach of duty to his own company that he has taken into account the benefit of the group as a whole.¹

Not dissimilar issues arise in relation to a nominee director who, notwithstanding their appointment at the behest of a parent,

shareholder or creditor, owes his duties to the company of which he is appointed as a director and not to the nominating entity.

Where a person or entity is a director of two companies and there is a conflict between those two companies, it has been held that that person is "placed in an impossible position" and cannot discharge his duty to at least one company.² Where an actual conflict occurs, a director will have to cease acting for at least one company and preferably both.³

It follows from this that it is difficult to see how a director conforms to his director's duties if he knowingly delegates to a person who has an actual conflict of interest.

LIMITS OF DELEGATION

Even if the company has adopted the Model Articles (or Table A), the articles should be closely considered to see if there are any additions or amendments inconsistent with the general permission to delegate.

Further, as a matter of law, not all acts can be delegated and it will be necessary to consider the contextual legal framework to ensure that delegation is permitted. For example, the power of directors to authorise a director's conflict of interest in a matter is governed by s 175 of the Companies Act 2006. Section 175(4)(b) provides that it is for the directors to authorise any conflict and the subsequent subsections prescribe the procedure. It is considered that the statutory framework prohibits a delegation of the power to authorise a director's conflict of interest.

EFFECT ON THIRD PARTIES

A delegate will have actual authority to exercise certain functions of the board. This may extend to the power to contract on behalf of the company although special rules apply to deeds (s 44 of the Companies Act 2006).

Where the delegate transacts within his authority, the transaction will be binding on the company. However, third parties' ability to rely on acts by the delegate will not be limited to those made within the delegate's actual authority. Applying the usual rules of apparent or ostensible agency, third parties will also be able to rely on acts

entered into by the delegate if the company, by words or conduct, represents or permits it to be represented to the third party that the delegate has authority to act on the company's behalf even if the delegate did not in fact have authority to do so.⁴

In addition, a series of cases in the 19th and early 20th century give support for the view that, if the company's articles provide for delegation of an act to a person and that person purports to do that act, then a third party is entitled to assume that person had authority.⁵ This has been rationalised as a form of implied actual authority.⁶

CONCLUSION

It will be vital for a director whose board does delegate lawfully to ensure that delegation does not equate to abdication. Whilst circumstances will vary, it will normally be appropriate to agree and implement a monitoring procedure of the delegate. Some internal checks on the delegate's authority might be appropriate (even if a third party would not be bound by such limits). ■

- 1 See comments of Pennycuik J in *Charterbridge Corp v Lloyds Bank Ltd* [1970] Ch 62.
- 2 *Meyer v Scottish Cooperative Wholesale Society Ltd* [1959] AC 324, HL.
- 3 *Bristol and West Building Society v Mothew* [1998] Ch 1 at p 19.
- 4 *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480.
- 5 *Dey v Pullinger Engineering Company* [1921] 1 KB 77.
- 6 *Bowstead & Reynolds on Agency* at paras 3-028 to 3-030.

Further Reading:

- Authorising multiple directorships in unrelated companies: Table A to the rescue? (2011) 9 JIBFL 534.
- Dealing with directors' conflicts of interest under the Companies Act 2006 (2008) 6 JIBFL 292.
- LexisPSL: Company: Practice Note: Directors' decision-making: power, authority and duties.