# NO LONGER OFF THE HOOK: CONSEQUENCES OF THE BREACH OF DIRECTORS FIDUCIARY DUTIES

## INTRODUCTION

It is trite that Companies are juristic entities existing separately from their members. Hence, they can sue or be sued, hold assets and incur liabilities. In recent times however, directors have been known to incur personal liabilities deriving from a Company's acts or omissions.[1]

The dynamic corporate landscape in Nigeria relies on the effective corporate governance and decision-making of company directors. Directors are entrusted with significant power and responsibility, and act as fiduciaries who must uphold the highest standards of loyalty, care, and good faith in their duties towards the company. However, the breach of fiduciary duties by directors has become a prevalent issue, raising concerns about accountability and the protection of shareholders' interests, and regulatory requirements.

An example is the circular released by the Corporate Affairs Commission ("CAC") on the 2nd of November 2023 informing company directors and officers that from the 1st of January 2024, the full penalties prescribed in the **Companies Regulations 2021** ("**the Regulations**") shall be applied for the failure to file annual returns. **Section 425 (1) of the Companies and AlliedMatters Act (CAMA) 2020** provides that:

> **"If a company required to comply with any of the provisions of sections 417 – 423 fails to do so, the company <u>and every director or officer of the company</u> are liable to a penalty as may be prescribed by the Commission".**

This article delves into the issue of breach of fiduciary duties by directors in Nigeria, the far-reaching consequences of the breach of these duties, and the steps that can be taken by directors and shareholders to curb a breach of these duties.

## CONSEQUENCES FOR BREACH OF FIDUCIARY DUTIES

The consequences of a director's breach of his fiduciary duties towards the company includes:

1. **Legal Actions:** Shareholders, regulatory authorities, and the company itself may initiate legal actions against the breaching directors. This can lead to civil liability and damages.

[1] Salomon v. Salomon [1897]. AC 22.

2. **Disqualification:** A director's breach of duties may result in his being disqualified from serving on boards of other companies in the future. **Section 283 (d) of CAMA** provides that:

> **"a person disqualified under sections 279, 280, 284 of this Act shall be disqualified from being a director".**

While **section 280(1) of CAMA** provides that:

> **"where a person is convicted by a High Court of any offence in connection with the promotion, formation or management of a company…….the court shall make an order that that person shall not be a director of or in any way, whether directly or indirectly, be concerned or take part in the management of a company for a specified period not exceeding 10 years."**

The implication of the above is that a director that breaches his fiduciary duty to manage, promote, and form a company, and commits an offence in the process will be prohibited from becoming a director in that company and in another company for a period not exceeding 10 years.[2]

3. **Regulatory Sanctions:** Regulatory authorities may impose additional sanctions, including fines or penalties, on directors who breach their fiduciary duties. They may also be required to pay financial penalties or damages to compensate the company or its shareholders for any losses incurred due to the breach. CAMA and the Regulations expressly prescribe the types of penalties for different failures of a director and company to perform their duties. They prescribe daily default fees on the directors and companies in instances such as failure to issue all unissued shares[3], and a one-off default for instances such as the failure to file annual returns.
The implication of the penalties prescribed by the Regulations is that each director will be personally liable in addition to the company for the company's failure to file annual returns. To prevent same, it is pertinent that directors ensure the timely filing of their company's annual returns.

[2] Section 280(1) CAMA
[3] Regulation 14- Company Regulation 2021.

4. **Criminal Charges:** In cases of serious misconduct and egregious breach, directors may face criminal charges for offences, such as fraud[4], or false statements. Section **280(1) of CAMA** in addressing the issue of fraud provides that:

> **"Where— (a) a person is convicted by a High Court of any offence in connection with the promotion, formation or management of a company, or**
> **(b) in the course of winding up a company, it appears that a person—**
> **(i) has been guilty of any offence for which he is liable (whether he has been convicted or not) under sections 668 – 670 of this Act, or**
> **(ii) has been guilty of any offence involving fraud,**
> **the court shall make an order that that person shall not be a director of or in any way, whether directly or indirectly, be concerned or take part in the management of a company for a specified period not exceeding 10 years.**

**Section 862(1)(a) of CAMA** in addressing the issue of false statements provides that:

> **"…if any person in any return, report, certificate, balance sheet, or other document required by, or for the purpose of any of the provisions of this Act, willfully makes a statement which is false in any material particular knowing it to be false, he commits an offence and is liable — (a) on conviction to imprisonment for a term of two years;…"**

5. **Reputational Damage**: Breaches of fiduciary duty can lead to significant reputational damage for directors, which can affect their future career opportunities and relationships within the business community.

6. **Board Removal:** The board of directors and/or shareholders may vote to remove a director who has breached their fiduciary duties.[5]

## FIDUCIARY DUTIES OF DIRECTORS

In Nigeria, the fiduciary duties of directors are primarily derived from common law and statute. The fiduciary duties include:

[4] Section 280 CAMA
[5] Section 288 CAMA

1. **Filing Annual Returns:** Company directors are responsible for ensuring their company's compliance with all relevant laws and regulations, including but not limited to regulatory returns being filed timely. Compliance with laws and regulations on filing of annual returns is a critical responsibility for companies and should be overseen by their directors as they can be held personally liable along with the company for failure to do same.

   The Regulations prescribes the one-off default payment for each director's and the company for each annual return not filed.

2. **Loyalty:** Directors have a duty to act in the best interests of the company and its shareholders. Directors should avoid conflicts of interest and avoid personal gain. **Section 305(3) of CAMA** reiterates this point by stating that:

   > **"A director shall act at all times in what he believes to be the best interests of the company as a whole so as to preserve its assets, further its business, and promote the purposes for which it was formed, and in such manner as a faithful, diligent, careful and ordinarily skillful director would act in the circumstances and, in doing so, shall have regard to the impact of the company's operations on the environment in the community where it carries on business operations"**

   The duty of directors to be loyal to the company by acting in the best interest of the company cannot be overemphasized, as failure to uphold same exposes directors to the consequences of non-compliance.

3. **Duty of Care and Skill**: Directors are required to exercise reasonable care, skill, and diligence in their roles, making informed decisions and staying well-informed about the company's affairs.

   **Section 308 of CAMA** provides that:

   > "**Every director of a company shall exercise the powers and discharge the duties of his office honestly, in good faith and in the best interests of the company, and shall exercise that degree of care, diligence and skill which a reasonably prudent director would exercise in comparable circumstances."**

The court in espousing the level of care and skill required of directors stated in **Lagunas Nitrate Co. v. Lagunas Syndicate**[6] that:

> **"if directors act within their power, if they act within such care as is reasonably expected from them, having regard to their knowledge and experience, and if they act honestly for the benefit of the company they represent, they discharge both their equitable as well as their legal duty to the company."**

The consequence of failure of a director to take reasonable care and act with reasonable skill is a ground for an action for negligence and breach of duty.[7]

4. **Duty to Manage the affairs of the Company**: **Section 269 of CAMA** defines a director as a person duly appointed by the company to direct and manage the business of the company. **Section 87(3) of CAMA** provides that:

> **"…except as otherwise provided in the company's articles, the business of the company shall be managed by the board of directors who may exercise all such powers of the company as are not by this Act or the articles required to be exercised by the members in general meeting. "**

Also, In ***Artra Industries Nig Ltd v. The Nigerian Bank for Commerce and Industry***[8]**,** the court held that directors must adhere strictly to the statutory provisions which enjoins them to consider the interest of the company as paramount.

5. **No Secret Profit/Undisclosed Benefit:** Secret profit is a financial gain, benefit or advantage which a director obtains in connection with the company's affairs without the knowledge and approval of the company or its shareholders. **Section 306 (2)** of CAMA provides that a director shall not:

> **"(a) in the course of management of affairs of the company, or**
> **(b) in the utilisation of the company's property,**
> **make any secret profit or achieve other unnecessary benefits."**

The position on the duty not to make secret profit is further espoused in the case of ***Regal Hasting Ltd. V. Gulliver***[9] which lends credence to the fact that a director is

[6] [1899] 2 Ch 392.
[77] Section 308(2) CAMA
[8] [1988] 4 NWLR (Pt.546), 357.
[9] [1942] 1 All ER 378; [1972] 2 A.C 134.

prohibited from making any undisclosed benefit, and the breach of this duty exposes him to legal consequences.

## CONCLUSION

Corporate governance is pivotal to a Company, and directors are entrusted with managing companies for the benefit of shareholders. The breach of their fiduciary duties does not only threaten the financial stability and reputation of the company, but also undermines the confidence of investors and the public in the corporate sector. As such, understanding the dynamics and implications of these breaches is essential to promoting transparency, integrity, and responsible corporate leadership.

We recommend that directors invest in a good corporate governance structure to place checks on their fiduciary duties to the company. Directors should engage the services of legal practitioners, or a company secretary with legal background who is vast on the subject of corporate governance to ensure legal compliance with the MEMART of the company, and the extant laws on corporate governance.