

Chapter 9

The Role and Powers of the Board

Here, basic guidance to the end-of-chapter questions will be provided.

1. Define the following terms:

- quorum;
- minutes;
- reserve power;
- casting vote.

| Term | Definition |
|---------------|--|
| quorum | The minimum number of qualifying persons required to be present in order to transact business |
| minutes | The formal record of a meeting |
| reserve power | A power granted to the members to direct the directors to take, or refrain from taking, specified action |
| casting vote | A vote granted to a person to determine a vote where the result is tied |

2. State whether each of the following statements is true or false and, if false, explain why:

- **the model articles provide that the directors may exercise all the powers of the company, and so the members cannot interfere in management;**
- **the directors' powers of management will revert back to the members if the directors refuse to attend board meetings;**
- **the articles of most companies do not specify how much notice must be provided for a board meeting;**
- **if the articles do not state what constitutes a quorum, then two directors will constitute a quorum;**
- **the directors may only delegate their powers if the articles so allow.**

- **The model articles provide that the directors may exercise all the powers of the company, and so the members cannot interfere in management:** This statement is false. Whilst art 3 of the model articles does indeed provide the directors may exercise all the company's powers, art 4 allows the members to interfere in management by passing a special resolution ordering the directors to take, or refrain from taking, specified action.
- **The directors' powers of management will revert back to the members if the directors refuse to attend board meetings:** This statement is true.
- **The articles of most companies do not specify how much notice must be provided for a board meeting:** This statement is true.
- **If the articles do not state what constitutes a quorum, then two directors will constitute a quorum:** This statement is false. If the articles do not specify what constitutes a quorum, then a majority of directors will constitute a quorum.

- **The directors may only delegate their powers if the articles so allow:** This statement is true.

3. 'In most companies, the division of power between the directors and the members is excessively unbalanced in favour of the directors.' Do you agree with this quote? Provide reasons for your answer.

Introduction

- Every essay should begin with a succinct introduction that demonstrates that you understand the essay question. Briefly explain what the essay is about and set out what the essay will discuss and how it will be structured.
- This question requires you to discuss the balance of power between the board and the members.

The balance of power

- Begin by pointing out that the default position is that the power to manage a company is vested in the members. In small private companies, the members may indeed manage the company (such members will also be directors).
- However, in larger companies, it will not be realistic for the members to management company and so the members usually delegate their managerial power to the directors via the articles.
- This is reflected in art 3 of the model articles, which provides that '[s]ubject to the articles, the directors are responsible for the management of the company's business, for which purpose they may exercise all the powers of the company.'
- The articles of most companies will contain a provision similar to that found in art 3 and so it is clear that a significant amount of power is vested in the directors. The question is to what extent can the members still exercise, or interfere in, managerial power. This requires us to discuss the members' delegation of power to the directors.

The members' delegation of power to the directors

- As noted, in the vast majority of companies, the members delegate managerial power to the directors. However, it is an unusual form of delegation in that, once the members delegate their managerial powers to the directors, the members lose the right to interfere in management unless the articles allow them to do so (see e.g. *Automatic Self-Cleansing Filter Syndicate Co Ltd v Cuninghame*).
- As a result of this, the balance of power is often shifted significantly in favour of the directors. However, this managerial power can be affected or limited by the articles (art 3 specifically states that the power of the directors to manage is 'subject to the articles'). As a result, the articles can be amended to provide the members with the ability to interfere in management (see e.g. *Salmon v Quin & Axtens Ltd*).
- A notable example of this is found in art 4 of the model articles which provides a 'reserve power' to the members and states that the members may, by passing a special resolution, direct the directors to take, or refrain from taking, specified action. Of

course, a related issue here is the extent to which the members can exercise this reserve power. In smaller companies where the directors will often be majority shareholders, minority members will be unable to exercise such a power. In larger companies, the exercise of such a power is almost unheard of.

Conclusion

- Every essay should end with a conclusion. Briefly summarise the main points/arguments and, if possible, come to a conclusion regarding the essay topic (i.e. which of the opposing views has the stronger arguments).

4. Dragon Tools Ltd ('DT') has adopted the model articles for private companies, but has added an additional article, namely 3A which provides that 'any decision of the directors that involves expenditure of over £10,000 requires the approval of Dragon plc' (DT's parent company). DT's directors decide to acquire a piece of land on which to build a new factory. Belinda, the CEO of DT, is authorised to conclude an agreement for the purchase of the land and, on behalf of DT, she enters into negotiations with LandCorp Ltd to purchase a piece of land.

A board meeting is convened to discuss the possible purchase of the land. However, two directors attend, namely Belinda and Walter. Ahmed could not attend as he was away on company business, and Yvonne did not attend as she claimed she was not informed of the meeting. At the meeting, Belinda tells Walter that the £50,000 price is a bargain and DT should purchase the land immediately as a delay could risk the land being sold to someone else. Walter agrees and they pass a board resolution agreeing to purchase the land, and another resolution authorising Belinda to enter into the sale agreement on behalf of DT. A contract is entered into between DT and LandCorp. Dragon's approval was not obtained.

The board of Dragon plc hears of the purchase of the land and also discovers that Walter is a majority shareholder of LandCorp. Dragon seeks your advice on whether the contract between DT and LandCorp can be avoided.

- The two key issues here are (i) whether the resolutions passed at the board meeting were properly passed, and; (ii) does Belinda have authority to enter into the contract with LandCorp on behalf of DT.

The board meeting

- At a board meeting, resolutions were passed to purchase the land and to authorise Belinda to enter into a sales agreement on behalf of DT. The issue here we need to consider is whether these resolutions were valid.

Notice of the meeting

- Directors must be provided with notice of a directors' meeting, with the rules relating to notice being a matter for the articles.
- Yvonne stated that she was not informed of the board meeting. The general rule is that if due notice of a directors' meeting is not provided, then the meeting is invalidated (*Young v Ladies Imperial Club Ltd*). Accordingly, if Yvonne wishes to object to the lack of notice, she can do so, but she must do so immediately or the objection will fail (*Browne v La Trinidad*).

The requirement of a quorum

- There is another potential issue, which is that in order to validly conduct business, a directors' meeting must be quorate (i.e. it must have a quorum). What amounts to a quorum is a matter for the company's articles, with art 11(1) of the model articles for private companies stating that no proposal can be voted on if a quorum is not present (except a proposal to call a further meeting).
- Article 11(2) states that a quorum can be fixed from time to time by a decision of the directors and, unless otherwise stated, it will be two.
- Two directors, Belinda and Walter, attended the meeting. Accordingly, if DT's articles contain a provision similar to art 11, it would be assumed that a quorum is present.
- However, the courts have stated that only directors entitled to vote on a matter will count towards the quorum (*Re Greymouth Point Elizabeth Railway and Coal Co Ltd*) and there is debate as to whether Walter is entitled to vote.
- Walter is the majority shareholder of LandCorp. It is common for the articles to provide that, if a director is interested in a proposed transaction or arrangement, that director will not be counted as participating in the decision-making process for quorum or voting purposes, and such a provision is found in art 14(1) of the model articles states this. Accordingly, based on this, Walter would not count towards the quorum, meaning that the directors' meeting would be inquorate.
- However, the articles can specify ways in which a director such as Walter could count towards the quorum. So, for example, art 14(3)(a) provides that art 14(1) can be disapplied by the company passing an ordinary resolution.

Walter's conflict of interest

- A further point to consider is that, as Walter has an interest in the contract between DT and LandCorp, he must disclose this interest to the other directors before the transaction is entered into, and a failure to do so will be a breach of the duty in s 177 of the CA 2006.
- Once the transaction is entered into, if he continues to not disclose his interest, he will breach s 182 which imposes criminal liability.

Belinda's authority

- Belinda has purported to enter into a contract on behalf of DT with LandCorp. There are two potential issues here.

The inquorate meeting

- If the board meeting was held to be inquorate, then the resolution empowering Belinda would have no validity. In which case, Belinda would not have authority to enter into the contract.

Article 3A

- Even if the meeting was quorate, Belinda still does not have authority as art 3A requires the approval of Dragon plc. As a result, she would be in breach of the s 171(a) duty to act in accordance with the company's constitution.

Enforcement of the agreement

- LandCorp could try and enforce the agreement using s 40 of the CA 2006.