Volunteering as a director of a freehold company

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This guide by Commercial Solicitor, Alexander Willingham, and Leasehold Solicitor, David Gibson discusses the things to think about before taking the plunge, including what the role of a director includes and the duties and responsibilities they need to consider.

Becoming a director of a freehold company

Whether you've just been involved in buying the freehold of your block of flats or you've acquired a property in a building run by a freehold company that you are a shareholder in, you may well have the opportunity to become one of the directors of that company and help shape decisions about how your building is run. For some people, being a director is something they've been involved in in another capacity; through work or volunteering, but for others it's something they may never have even thought about before.

We aim here to give you an initial steer on what being a director of a freehold company involves, and whether there are any pitfalls to be aware of.

The Pros

1) You have more control

Or at least you have more control than you would without being a director. Usually a company is operated by the directors making decisions and signing off contracts and other paperwork on the company's behalf. As a director you would have a say in all of these decisions.

2) You can improve things for your block

If you feel the current board don't do enough in a particular area (for example some new owners found out about issues with the building when they purchased that they wish to see addressed for the benefit of their own flat and the others) then you would be able to flag this up to the other directors and press for it to be dealt with.

3) Necessity

A company needs directors to work properly, and if the past directors have moved away or died, someone has to make sure your building works properly, or it can impact your own experiences and even the value of your property if it were mismanaged. Importantly, if the company fails to make filings at Companies House on time it can result in the company being struck of the register there. If that happens and the owners aren't able to make an application to get it reinstated in time it can mean the freehold falls into he ownership of the Crown, and the owners would have to buy it back again.

The Cons

1) It's unpaid work

Usually you won't be able to draw a salary for the time you spend dealing with running your block. On the average day that might not feel like a problem, but if you end up in the midst of dealing with a dispute about the property, or have to pick up a lot of administrative slack for other directors who aren't as committed to their jobs as they should be, or even fall ill or pass away, you might feel like you've taken on a second job with no salary.

2) You may have to be the "bad guy"

You'll be wholly or partially responsible for deciding how the company deals with financial decisions like how much to spend on repairs and insurance, what it does about some owners not paying necessary sums on time (like maintenance and insurance costs), and giving decisions on what to do about disputes between neighbours or permissions for owners to carry out work to their flats. Needless to say not everyone will agree with the decisions you make or be very happy with the bills they are sent, so while you may find yourself more popular with some neighbours, you could find yourself having to be involved in disputes (or even legal proceedings) against others in order for the block to be properly run.

3) You have duties to the company

We set out advice below on the duties you'll often acquire by taking on the role. As you'll see, the job needs to be done properly, or it can have some significant consequences for you. Sometimes it's possible to take out directors liability insurance to cover the risks of a decision that goes wrong, which may well be something you push for as a new director!

What do Directors do?

Company directors typically run the operations and management of a company, in doing so they need to adhere to the company's constitution. The board of directors will usually meet and take decisions collectively on any given matter.

The seven duties noted below are often referred to as the 'General Duties'. This is because they are closely linked to the general duty to promote the success of the company.

General Duties

(1) To act within powers

A director must act in accordance with the company's constitution and exercise those powers within the limits for which they were granted.

(2) To promote the success of the company

A director must act in the way they consider would be most likely to promote the success of the company. The director must consider the following (non-exhaustive list):

- The likely consequences of any decision in the long term.
- 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 the environment.
- The desirability of the company maintaining a reputation for high standards of business conduct.
- The need to act fairly between members/ shareholders of the company.

(3) To exercise independent judgment

A director is required to exercise their own independent judgment.

(4) To exercise reasonable care, skill and diligence

A director must exercise the care, skill and diligence which would be exercised by a reasonably diligent person.

(5) To avoid conflicts of interest

A director must avoid situations in which they have a conflict with the company's interests.

(6) Not to accept benefits from third parties

Directors must not accept any benefit (including a bribe) from a third party.

(7) To declare any interest in a proposed transaction or arrangement with the company

Where directors are in any way directly or indirectly interested in a proposed transaction or arrangement with the company, they must declare to the other directors the nature and extent of that interest.

What are the consequenses of a breach of directors duties?

Directors owe duties to the company; and a breach of those duties could result in the company taking action against a director as follows (non-exhaustive list):

- a director being held personally liable to pay damages to the company;
- an injunction to force the director to do (or stop doing) something that is breaching their duties;
- a transaction the company has signed up to being undone, or a contract they have entered into being ended by a court; and
- a director being required to account for any profits made from a transaction or restore any company property affected by a breach.

Directors' responsibility on Insolvency

Directors of companies experiencing financial concerns face additional obligations. Directors may be liable for fraudulent or wrongful trading if the company continues trading when insolvent and the interests of creditors are prejudiced. Importantly, where a company is insolvent or approaching insolvency, the general duty to promote the success of the company is altered so that a director must instead act in the best interests of the company's creditors.

It is advisable to seek legal advice as soon as encountering financial difficulties to avoid potential personal liability in cases of insolvency.

Mitigating Director's Liability

Considering the above from the outset, directors should seek to understand the extent and scope of their role, obtaining timely and relevant legal advice where required is key along with keeping up to date with commercial developments.
In some cases, directors may be able to mitigate their liability. In certain situations, the court may grant relief from liability if the director has acted honestly and reasonably. In other circumstances, the shareholders of the company may ratify unauthorised acts.

Furthermore, a company may indemnify directors against certain actions brought against them.

Finally, it is important to note that a company may choose to take out directors' and officers' insurance. A policy such as this typically deals with directors' liabilities arising from claims of negligence, breach of duty or other default. Standard policy exclusions include fraud, dishonesty and criminal behaviour. Whatever policy is considered the directors should ensure they understand the limitations.

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