

Directors' Duties in the Isle of Man

Following the recent widely publicised case of the *Financial Services Authority v Irving & Irving*, director's duties in the Manx jurisdiction have been a matter of more public interest than other fiduciary relationships.¹ In this case, the Defendants were subject to an application for their disqualification as directors (which was subsequently ordered) after an octopus-like series of litigation relating to the dismissal of an attorney-general and a costs order being made against a well established Manx advocate, as well as Mr Irving Snr and Mr Irving Jnr being disqualified as directors for 8 and 7 years respectively. The reasons for the Irvings' disqualifications will be further explored below, but they range from failing to meet statutory filing obligations to entering the company into transactions for their personal, rather than the company's, benefit. While company law in the Isle of Man is generally divided between those constituted under the Companies Act 2006 and those constituted under certain acts prior thereto (commonly though somewhat erroneously known as "1931 act companies" due to the first act in that set), directors' duties in the small offshore jurisdiction are largely established by common law but some more specific duties are set out in statute. As a broad overview these duties are regulated by both the law of principal and agent as well as the equitable principle of fiduciary duties. These duties in practical terms are set out in an Isle of Man Government Guidance Note on the Responsibilities and Duties under the Laws of the Isle of Man (2007) as: loyalty to the company, obedience to the company's constitution, maintaining independence in decision-making, to not make a secret profit, to avoid a position of potential or actual conflicts of interest, to act with care skill and diligence and overall act with fairness in the management of their company.² It might be instructive that it is in particular transgressing their duties in relation to non-payment of tax and loyalty to the company that the court seems most affronted by in the *Irving* case despite the often sensationalised image of the Manx jurisdiction being one of tax avoidance and it being a utopia populated by the freewheeling ultra rich!

In the Isle of Man, a limited company is a separate legal entity from its directors. This therefore limits the liability of directors for a company's actions, but directors may expose themselves to personal liability by breaching their directorship duties as, for example, they would be liable to the company for damages resulting from their negligence.³ It is notable that the duties are owed to the company itself, not the shareholders or any beneficial owners. The directors therefore must act in

¹ *FSA v Irving & Irving* CHP13/130 found at <https://www.judgments.im/content/J2001.htm>

² Found at <https://www.gov.im/lib/docs/ded/companies/companiesReg/practicenotes/pn62007directors.pdf>

³ There are further exceptions to the limitation of personal liability in terms of the offences of fraudulent trading and misfeasance in both 1931 and 2006 companies acts, as well as unlawful distribution in the 2006 act only but these will not be dealt with in depth here as they can be seen more as criminal acts rather than a civil breach of a duty.

compliance with their standard of care in relation to the best interests of the company – meaning in practical terms, for example, they do not recommend a dividend is paid if they do not see that there are adequate finances in the company and paying such a dividend may result in the company’s insolvency. The standard of care required of a director is based on two tests, one objective and one subjective but in both tests they must be “reasonable diligent”. Respectively the tests are if the director has acted to a standard of care expected of a reasonably diligent person:

- Acting with the general knowledge, skill and experience that may reasonably be expected from a person carrying out the same functions as are carried out by that director in relation to the company (objective test), and
- Acting with the actual general knowledge, skill and experience that that director personally has (subjective test)⁴

These tests do not however provide an excuse for ignorant directors – the Isle of Man Financial Services Authority’s (“FSA”) guidance provides that if directors are in doubt they should seek professional advice.⁵ Further, an individual director’s duties form part of the collective whole of the board’s duties, and in relation to this a director should keep the board well informed so they will best perform their duties.⁶ The standard of care directors in the Manx jurisdiction is therefore multi-faceted – it contains an obligation to be diligent but also to be diligent in knowing one’s own limits, to act in accordance in his/her own ability but also to act in accordance with the ability of a director in a similar position, and to make sure he/she acts in accordance with his/her own individual duties but also make efforts to ensure the board’s collective duties are also complied with. Returning to the examination of the *Irvings* case, the court refers to the “incompetence” of the Defendants in not performing one of their statutory obligations as directors. In this way it can be seen that the Manx High Court sees the standard of care and statutory obligations of directors not as two different sources of obligations but two sides of the same coin.⁷

In addition to the standard of care, a central obligation on a director of a Manx company is the fiduciary duty to act bona fide in the interests of the company and with a proper purpose. Within this is the obligation to avoid a position of an actual or potential conflict between their personal interests and their duties to the company. It is notable however that despite the above-mentioned duty not to make a secret profit, a director of a 2006 act company may be allowed to retain the benefit from an interest in a transaction provided that he/she has disclosed his interest to the board prior to the

⁴ Appleby – Guide to Directors and Their Duties in the Isle of Man (February 2015) at <https://www.applebyglobal.com/publication-pdf/guide/guide-to-directors-and-their-duties-in-the-isle-of-man---february-2015.pdf>

⁵ Isle of Man Financial Services Authority – Financial Services Act 2008 and Guidance on the responsibilities and duties of directors under the laws of the Isle of Man (January 2017) at <https://www.iomfsa.im/media/1699/guidanceontheresponsibilitiesand.pdf>

⁶ Appleby, *Ibid.*

⁷ *FSA v Irvings, Ibid.*

transaction being made in accordance with sections 103 to 105 of the 2006 Act. Despite this, a director must ensure that they maintain independence in assessing whether any transaction would be for the benefit of the company and particularly not be bound by any third party obligations in relation to their decision-making. Central to this is the principle that a company is a separate legal entity, which, while it affords the benefit of limited liability to the owners and directors, means that a company must not purely be a vehicle for a dominant director to benefit him or her-self. This is a thread that runs through the issues the court found with the Irvings' conduct in their use of a company in order to benefit themselves rather than the company. In particular, the judgment states:

“Given the way in which assets were passed around the various companies it is not clear to me that the Defendants ever understood the concept of corporate personality [...] [concerning a transaction involving an apartment] That was a misapplication of SHL's funds for the benefit of Mr Irving personally and in breach of his duty to SHL”

The presiding Deemster later states that a disqualification order is necessary partially in order to regulate the abuse of limited liability.⁸

The Manx jurisdiction has a series of duties imposed on the directors of Manx companies but arguably retains a level of flexibility in enforcing the said duties. It is, on the one hand, well advised for directors to brief themselves on their duties as set out in various government department's/statutory bodies' notes, but the duties as discussed above should not be so onerous that a layman is dissuaded from wanting to start and manage his own company from a scratch. The central theme running through directors' duties in the Isle of Man could be seen to encourage good, flexible and honest business in order to benefit firstly the company. The benefits of limited liability for a natural person is therefore not afforded freely, that is to say a person cannot manage a company purely to directly provide himself wealth and limit his/her liability but must ensure his/her company continues to exist as a solvent separate legal entity. It is unlikely that directors' duties could be seen as unfairly onerous on the individual, and rather they help provide assurance to those trading with the Island that the corporate body they are trading with will not suddenly be dissolved by a rogue director seeking to enrich himself solely from the company's success. The tests imposed on directors in terms of their standard of care and fiduciary duties, much like the larger English/Welsh jurisdiction neighbouring the Island, allow for both a stringent test on the actions of the director as an individual, as well as ensuring that their diligence is in line with what is expected from directors of Manx companies generally. Manx law, therefore, retains a desirable balance between opening opportunities up to the layperson, while also making sure directors of Manx companies are bound by high standards.

⁸ *FSA v Irvings, Ibid.*