"BRIEFING AGAINST THE BOARD": WHEN DISRUPTIVE DIRECTORS RISK BREACHING THEIR DUTIES

The English High Court judgment in *Stobart v Tinkler* concerns how the Board of a FTSE 250 infrastructure company, Stobart Group, fractured in 2018 following the actions of a dissenting director who sought to turn shareholders against the Board.

As well as offering an insight into the damaging effect conflict between directors can have on the governance of a company, the case highlights key considerations for all boards and directors when complying with their duties.

BATTLE IN THE BOARD ROOM

The dispute in *Stobart Group Limited v Tinkler* [2019] EWHC 258 (Comm) emerges from the high-profile and colourful conflict between the majority of Stobart's directors on the one hand, and a dissenting executive director with significant shareholder support, Mr Tinkler, on the other.

At its core, the dispute concerned actions taken in 2018 by Mr Tinkler as part of a "personal campaign" to remove Stobart's Chairman, Iain Ferguson. Fuelled by a grievance over his level of remuneration, Mr Tinkler took various steps to agitate for the removal of Mr Ferguson, including: (i) criticising the Board's management in discussions with shareholders, "behind the back of the Board"; (ii) sending what the Judge considered to be a "seriously misleading" and "disgraceful" letter to Stobart's shareholders encouraging them not to re-elect Mr Ferguson at the upcoming AGM on 6 July 2018; (iii) forwarding this letter to Stobart's employees to encourage them to turn against the board; and (iv) sharing confidential information with a shareholder about a potential deal.

These steps, which His Honour Judge Russen QC described as "guerrilla tactics" designed to reassert Mr Tinkler's control over Stobart, were found to constitute a "serious" breach of the statutory and fiduciary duties owed by Mr Tinkler to Stobart as a director, and amounted to a breach of his service contract as an employee.

The majority of the Board, backing the Chairman, also fell foul of their fiduciary duties by causing 5.3 million shares held in treasury to be transferred to Stobart's employee benefit trust shortly before the 6 July 2018 AGM, so that the scheme trustee could vote these shares in favour of Mr Ferguson's re-election as Chairman.

Thus, by the summer of 2018, the inner workings of Stobart's board had devolved into "thrust and counter-thrust between the rival camps".

Key points

- The duty on directors to act in the company's "best interests" means those of its shareholders as a whole, without discriminating between any majority or minority factions that might exist.
- The duty on directors to exercise independent judgement does not entitle a director to operate independently of the board in matters which fall within the management of the company's affairs.
- Directors should only discuss the management of a company's affairs with shareholders in the presence of the rest of the board or with their prior approval.
- Directors should proceed with caution in any discussions with shareholders to ensure that confidential information is not shared.

DUTY CALLS

In the course of deciding the key question in this case, namely whether Mr Tinkler's conduct was such as to justify his removal from Stobart's board and his dismissal as an employee, the Court gave some valuable insights on the proper functioning of a board of directors and the duties that directors owe:

1. **The duty to act in good faith and in the company's best interests.** It is a well-established principle that the company (in the ordinary course) is the sole beneficiary of a director's duties. In these circumstances, the company's "*best interests*" means those of its shareholders as a whole, without discriminating between the interests of any majority or minority factions that might exist (as reflected in s.172(1) of the Companies Act 2006). The Judge summarised this duty as follows:

   > "the duty upon a director to act in the best interests of the company therefore means just that. They are its human agents and have been entrusted by the shareholders to manage its affairs and protect its property"

   However, the Court did not believe that this precluded a company's directors from taking decisions in its best interests against the wishes of the majority of its shareholders. As such, Stobart's Board had not acted in breach of their duties by exercising their powers under the company's articles of association to remove Mr Tinkler as a director, even though he had been re-elected by the shareholders at the AGM the previous day.

2. **The duty to exercise independent judgement.** Mr Tinkler relied upon this duty to justify his actions in speaking separately to shareholders about his purported concerns about Stobart's management. Conversely, Stobart contended that these actions transgressed Mr Tinkler's duty to act in the best interests of the company, regardless of whether Mr Tinkler believed he was exercising his independent judgement.

   Mr Tinkler's rationale did not find favour with the Judge: he found that this duty did not entitle a director to do his own thing, independently of the board, in relation to matters which fall within the sphere of management of the company's business. Put simply:

   > "the duty upon each director to exercise an independent judgement exists in order to support the board's management of the company's business in an efficient and competent manner".

3. **The duty to act for proper purposes.** The Judge made it clear that, as a matter of principle, a decision of the Board which has not been taken for a proper purpose cannot be upheld on the basis it is perceived to be beneficial to the company.

   As such, although the majority of the board of directors believed that securing Mr Ferguson's re-election at the AGM was in the company's best interests, they had acted in breach of their duty to act for proper purposes by transferring shares to the employee benefit trust to swing the vote.

4. **The "sufficient information" duty.** The directors have a duty to provide shareholders with sufficient information to enable them to make an informed decision on any matter which falls to their vote at

an AGM. The Judge reiterated that this duty requires all shareholders to be provided with sufficient information, but it will not justify improper sharing of information with a select few shareholders.

5. **The collegiate function of the Board.** Given the fracture and infighting which plagued Stobart's board in spring/summer 2018, the Judge emphasised that when directors act they should do so collectively as part of the board of directors. A director cannot "short-circuit" the board (to which, as a whole, management of the company's affairs has been delegated, and of which one director forms only one part) by taking his issues over management directly to just some of the shareholders.

PRACTICAL LESSONS

This decision emphasises a number of important principles of good corporate governance and considerations for all boards and directors:

1. **The Board as the appropriate forum.** Where directors have concerns over the management of the company, these should always be raised with the board, rather than with shareholders, in the first instance.
2. **Discussions with shareholders.** Management matters of which a director has become aware by virtue of his/her position on the board should only be discussed with shareholders in the presence of the rest of the board or with their prior approval.
3. **Sharing of confidential information.** Directors should proceed with caution in any discussions with shareholders to ensure that confidential information is not shared inappropriately. For example, directors who sit as representatives of fund investors on portfolio company boards should be acutely aware of this risk when sharing information with fund investors, who may not be the only shareholders of the company.
4. **The "give and take" of board dynamics.** Directors should not feel duty-bound to adhere to the majority view. They should ensure that they keep appraised of the company's affairs and make their views known to other directors, whilst also listening to and taking account of the views of fellow directors.
5. **The minority view.** Where a director does not agree with a decision reached by the majority of the board, that director can legitimately defer to those views where he is persuaded that his/her fellow directors' views are advanced in what they perceive to be the best interests of the company, even if he is not himself persuaded of the decision. A minority director is not in any breach of duty or obliged to resign if he/she abstains from voting or explains that he/she defers to the views of his/her fellow directors, but he/she should raise this objection at the relevant board meeting and request that it is minuted.
6. **When to resign.** A director should consider resigning if he/she considers that a decision reached by the majority of the board is likely to be seriously detrimental to the company, and he/she has been unsuccessful in opposing it. This is particularly so where the director considers that there is a prospect of personally being held accountable for any resulting harm to the company or its creditors.

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