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Dear Adrian,

Thank you for your letter of 5 September, asking whether it would be possible under current law for a unitary board to turn itself into a two-tier board with the agreement of the shareholders. I have consulted DTI solicitors over the terms of this reply.

By way of background I should say that there is no definition of "board of directors" in the Companies Acts. Generally the Acts refer to "the directors". However the 1989 Act used the term "board of directors". Thus one now finds references to the board of directors, powers of directors, powers of the board, meetings of directors, and meetings of the board.

Traditionally the powers of management of a company have been handed to the directors by the articles of association, and there is considerable scope for dividing up the powers and functions of the directors by the articles route. One way to do this is through committees, and indeed Table A to the Companies Act (which sets out model articles) refers to directors delegating their powers in this way.

A further point of background is that company law imposes the same basic duties (eg of care and skill, and to act in good faith in the interest of the company) on all directors. These duties apply irrespective of whether the director is executive or non-executive, and irrespective of the number of committees of the board on which he sits. In considering whether a particular director had exercised care and skill, a court would not necessarily expect a non-executive director to exercise the same degree of care and skill as his executive co-director. A court would also not expect the same standard of care from a director of a local garage as from a director of multinational oil company. This does not however alter the basic duty that all directors have to exercise care and skill.

Turning now to your question, it is possible - in a very broad sense - for companies under current law to adopt two-tier board structures if they wish. As explained above, the Act

allows by the articles of association companies and in turn directors to organise their own internal structures largely as they wish. Individual directors or committees of directors may thus be allocated particular responsibilities. However under English law they remain "the directors", one organ of the company.

What one cannot say is that a committee structure under English law would meet a continental lawyer's view of a two-tier board. The continental view envisages two separate organs of the company, the supervisory board and the management board, with different legal responsibilities.

You go on to say that, if a statutory basis for a two-tier board were to be proposed, then the same would presumably have to be done for unitary boards. I agree with this, but I am not sure whether I agree with your subsequent comment that providing a statutory basis for unitary boards would be welcome. Business might appreciate the extra clarity but new legislation might also bring rigidities that would not be welcomed. There would also doubtless be wider political arguments which would depend on the overall package of reforms being proposed.

Your letter gives me the opportunity to let you know about some reforms on which the Department is working at present. If all goes well, they will be the subject of a consultation document that will be issued early in the new year. Among the main proposals are likely to be the following:

a) that there should a statutory statement of directors' duties to act in good faith in the interests of the company, and to exercise skill and care, on the face of the Companies Act. At present these duties are based on equitable principles and rules. The main purpose of the reform would be to make much clearer to directors what their duties are;

b) that there should also be a statutory rule on the face of the Companies Act to the effect that directors may not (other than by way of lawful remuneration) derive any personal benefit from any money or property of the company, or loan by the company. The Act would however allow shareholders to agree modifications to this rule via the articles of association;

c) that the current provisions in Part X of the Companies Act concerning loans to, and property transactions involving, directors should be repealed. Reliance would be placed instead on the general rule at (b). The current disclosure provisions would remain and indeed be strengthened in some ways but be simplified. The object of these changes would be to deregulate Part X of the Act and its accompanying schedules which are widely regarded as excessively complex.

These proposals would have various features that I think would go with the grain of the Committee's report - for example, making clearer to directors what their responsibilities are; and emphasis on disclosure to shareholders. Sarah Brown or I would be very pleased to make a presentation to the Committee once the consultation document has been published. However I should emphasise that it has not yet been agreed by Ministers.

If before then there are any aspects of the above which you would like to discuss with me or my solicitor colleagues, I should be happy to arrange a meeting.

Yours sincerely,

Nigel.

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Companies Division