

# De Facto Directors Shadow Directors

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# Objectives

- (1) To define *de facto* and shadow directors
- (2) To consider how *de facto* shadow directors may be identified
- (3) Understand consequences of being a *de facto* or shadow director



# Why Do We Care?

**Common Bond:** Ways of bringing persons who aren't *de jure* directors under the umbrella of what it means to be a director.

## Why Do We Care?

- To affix fiduciary duties upon persons who are not *de jure* directors;
- To disqualify persons from acting as directors;
- To plead that the Company is bound by the actions of X;
- To validate actions taken by a Company
- To make use of remedies available to liquidators and other office holders against those who are directors.



# (1) Definition: Companies Act 2006

## Section 250

*In the Companies Act, 'director' includes any person occupying the position of director, by whatever name called.*



# (1) Definitions: Case Law

## De Facto Directors

- Originally: Very narrow basis- formal defects in appointment, or overstaying their welcome
- Only more recently expanded to include those acting without formal appointment (of any sort):

*Re Lo-Line Electric Motors Ltd* [1988] 2 All ER 692, [1988] Ch 477 and *Re Hydrodam (Corby) Ltd* [1994] 2 BCLC 180 (endorsed by the Court of Appeal in *Re Kaytech International plc, Secretary of State for Trade and Industry v Kaczner* [1999] 2 BCLC 351)

# (1) Definitions: Case Law

## De Facto Directors

'No doubt they were not properly elected, and were, therefore, not *de jure* directors of the company; but that they were *de facto* directors of the company is equally beyond all question. The point I have to consider is whether the person who acts as *de facto* director is a director within the meaning of this section, or whether he can afterwards be allowed to deny that he was a director within the meaning of this section. I think he cannot. We are familiar in the law with a great number of cases in which a man who assumes a position cannot be allowed to deny in a Court of Justice that he really was entitled to occupy that position. The most familiar instance is that of executor *de son tort*. In like manner, it seems to me, in an application under this section, the *de facto* director is a director for the purposes of this section.'

Sir George Jessel MR *Re Canadian Land Reclaiming and Colonizing Co, Coventry and Dixon's Case* (1880) 14 Ch D 660

# (1) Definitions: Case Law

## De Facto Directors v Shadow Directors

I would interpose at this point by observing that in my judgment an allegation that a defendant acted as de facto or shadow director, without distinguishing between the two, is embarrassing. It suggests – and counsel's submissions to me support the inference – that the liquidator takes the view that de facto or shadow directors are very similar, that their roles overlap, and that it may not be possible to determine in any given case whether a particular person was a de facto or a shadow director. I do not accept that at all. The terms do not overlap. They are alternatives, and in most and perhaps all cases are mutually exclusive.

*Re Hydrodam (Corby) Ltd* [1994] 2 BCLC 180. (per Millett J)

# (1) Definitions: Case Law

## De Facto Directors

'A de facto director is a person who assumes to act as a director. He is held out as a director by the company, and claims and purports to be a director, although never actually or validly appointed as such. To establish that a person was a de facto director of a company it is necessary to plead and prove that he undertook functions in relation to the company which could properly be discharged only by a director. It is not sufficient to show that he was concerned in the management of the company's affairs or undertook tasks in relation to its business which can properly be performed by a manager below board level.

*Re Hydrodam (Corby) Ltd* [1994] 2 BCLC 180. (per Millett J)



# (1) Definitions: *De Facto* Directors

## De Facto Directors

*Some of the expressions used by Millett J in the Hydrodam case could be construed as meaning that, for a person to be held to have been a de facto director, the label 'director' must have been attached to him. But I am sure that Millett J did not mean that. He was concerned to distinguish between a de facto director and a shadow director, the latter being a person in accordance with whose directions or instructions the directors of a company (whether de jure or de facto) are accustomed to act.*

Warner J

**Re Moorgate Metals Ltd - [1995] 1 BCLC 503**

# (1) Definition: Companies Act 2006

(See Also: CDDA s.22(5))

## Section 251: ‘Shadow Director’

*(1) In the Companies Acts “shadow director”, in relation to a company, means a person in accordance with whose directions or instructions the directors of the company are accustomed to act.*

*(2) A person is not to be regarded as a shadow director by reason only that the directors act*

*(a) on advice given by that person in a professional capacity;*

*(b) in accordance with instructions, a direction, guidance or advice given by that person in the exercise of a function conferred by or under an enactment;*

*(c) in accordance with guidance or advice given by that person in that person's capacity as a Minister of the Crown (within the meaning of the Ministers of the Crown Act 1975)*

# (1) Definitions: Case Law

## Shadow Directors

A de facto director, I repeat, is one who claims to act and purports to act as a director, although not validly appointed as such. A shadow director, by contrast, does not claim or purport to act as a director. On the contrary, he claims not to be a director. He lurks in the shadows, sheltering behind others who, he claims, are the only directors of the company to the exclusion of himself. He is not held out as a director by the company.

*Re Hydrodam (Corby) Ltd* [1994] 2 BCLC 180. (per Millett J)

But this distinction is evaporating.



## (1) Definition: Shadow Directors

*Secretary of State for Trade and Industry v Deverell and another* -  
[2001] Ch 340

Morrison LJ

*The definition of a shadow director is to be construed in the normal way to give effect to the parliamentary intention ascertainable from the mischief to be dealt with and the words used. In particular, as the purpose of the Act is the protection of the public and as the definition is used in other legislative contexts, it should not be strictly construed because it also has quasi-penal consequences in the context of the Company Directors Disqualification Act 1986.*

## (2) Identification: De Facto Directors

### Objective Test

*A defendant does not avoid liability if he shows that he in good faith thought he was not acting as a director. The question whether or not he acted as a director is to be determined objectively and irrespective of the defendant's motivation or belief.*

*Smithton Ltd (formerly Hobart Capital Markets Ltd) v Naggar* [2014]  
EWCA Civ 939

Arden LJ

## (2) Identification: De Facto Directors

### De Facto Directors

*Re Lo-Line Electric Motors Ltd* [1988] 2 All ER 692, [1988] Ch 477 per Sir Nicolas Browne-Wilkinson V-C.

- R resigns but stays on as ‘production manager’ under nominal director;
- R carries on managing the business while remaining director leaves for USA;
- Doesn’t deny having managed the business.
- CDDA includes *de facto* directors: purpose is protection.

## (2) Identification: *De Facto* Directors

### De Facto Directors

*"The liquidator submitted that where a body corporate is a director of a company, whether it be a de jure, de facto or shadow director, its own directors must ipso facto be shadow directors of the company. In my judgment that simply does not follow. Attendance of board meetings and voting, with others, may in certain limited circumstances expose a director to personal liability to the company of which he is a director or its creditors. But it does not, without more, constitute him a director of any company of which his company is a director."*

*Re Hydrodam (Corby) Ltd* [1994] 2 BCLC 180. (per Millett J)

Okay, but what is 'something more'?

## (2) Identification: *De Facto* Directors

### De Facto Directors

It follows that I do not consider that the answer to the question on this appeal lies in considering what Millett J meant by the words 'without more,' and then attempting to catalogue what Mr Holland did. If the question is, as I believe, whether Mr Holland was part of the corporate governing structure of the composite companies and whether he assumed a role in those companies which imposed on him the fiduciary duties of a director, then I would answer that he was not.

Lord Collins

*Holland v Revenue and Customs Commissioners and another*

[2011] 1 All ER 430



## (2) Identification: *De Facto* Directors

### De Facto Directors

Warner J

#### **Re Moorgate Metals Ltd - [1995] 1 BCLC 503**

Held: R is a *De Facto* director. Factors include:

- Company founded by meeting invitation to H from R;
- Shared responsibility of management for H and R;
- R conducts unlimited trading for company;
- R consulted on all big decisions;
- Company literature describes R and H as ‘partners’.

## (2) Identification: *De Facto* Directors

### De Facto Directors

Jacob J

***Secretary of State for Trade and Industry v Tjolle* [1998]  
BCC 282**

*I think what is involved is very much a question of degree. The court takes into account all the relevant factors. Those factors include at least whether or not there was a holding out by the company of the individual as a director, whether the individual used the title, whether the individual had proper information (e.g. management accounts) on which to base decisions, and whether the individual has to make major decisions and so on. Taking all these factors into account, one asks 'was this individual part of the corporate governing structure?', answering it as a kind of jury question.*

## (2) Identification: *De Facto* Directors

### Ask: 'What Can't X Do'

Etherton J

*Secretary of State for Trade and Industry v Hollier and Others* [2006] All ER (D) 232 (Jul)

*While I can quite see that, as in Tjolle, a deliberate policy of preventing a person from gaining access to relevant information is likely to preclude a finding that such person was a de facto director, there may be circumstances in which it would be open to the court to find that a person who participated in corporate decisions on policy and strategy and in the implementation of such decisions was a de facto director, notwithstanding that he or she had no right to relevant information.*

## (2) Identification: Shadow Directors

*To establish that a defendant is a shadow director of a company it is necessary to allege and prove: (1) who are the directors of the company, whether de facto or de jure; (2), that the defendant directed those directors how to act in relation to the company or that he was one of the persons who did so; (3) that those directors acted in accordance with such directions; and (4) that they were accustomed so to act. What is needed is first, a board of directors claiming and purporting to act as such; and secondly, a pattern of behaviour in which the board did not exercise any discretion or judgment of its own, but acted in accordance with the directions of others.*

*Re Hydrodam (Corby) Ltd* [1994] 2 BCLC 180. (per Millett J)

## (2) Identification: Shadow Directors

*Secretary of State for Trade and Industry v Deverell and another* - [2001] Ch 340

Morrison LJ:

‘The purpose of the legislation is to identify those, other than professional advisers, with real influence in the corporate affairs of the company. But it is not necessary that such influence should be exercised over the whole field of its corporate activities...

(3) Whether any particular communication from the alleged shadow director, whether by words or conduct, is to be classified as a direction or instruction must be objectively ascertained by the court in the light of all the evidence. In that connection I do not accept that it is necessary to prove the understanding or expectation of either giver or receiver. In many, if not most, cases it will suffice to prove the communication and its consequence...

It appears to me that Judge Cooke, in looking for the additional ingredient of a subservient role or the surrender of discretion by the board, imposed a qualification beyond that justified by the statutory language.’

## (3) Consequences: Purpose

### Purposive Approach:

*In deciding this, one bears very much in mind why one is asking the question..... There would be no justification for the law making a person liable to misfeasance or disqualification proceedings unless they were truly in a position to exercise the powers and discharge the functions of a director. Otherwise they would be made liable for events over which they had no real control, either in fact or law.*

*Secretary of State for Trade and Industry v Tjolle* [1998] BCC 282

Jacob J

Can you simply ‘read-across’ definitions from one set of cases to another??

### (3) Consequences: Purposive Understanding

*It does not follow that 'de facto director' must be given the same meaning in all of the different contexts in which a 'director' may be liable. It seems to me that in the present context of the fiduciary duty of a director not to dispose wrongfully of the company's assets, the crucial question is whether the person assumed the duties of a director.*

Lord Collins

*Holland v Revenue and Customs Commissioners and another* - [2011]  
1 All ER 430

## (3) Consequences: Purposive Understanding

### Consequences

*Instant Access Properties Ltd (in liquidation) v Rosser and others; Murphy and another (as joint Liquidators of Instant Access Properties Ltd) v Rosser and others*

[2018] EWHC 756 (Ch)

- Common ground that *de facto* directors owed same duties as *de jure*

Morgan J

*It seems that a de facto director is in the same position as a de jure director. In a case where, for example, the individual is a de facto director because of a defect in his appointment as a de jure director and he acts as a director, then it seems reasonable that the de facto director should owe the full range of duties of a de jure director.*

But what if that isn't the case??



## (3) Consequences: Purposive Understanding

### Consequences

*Instant Access Properties Ltd (in liquidation) v Rosser and others; Murphy and another (as joint Liquidators of Instant Access Properties Ltd) v Rosser and others*

[2018] EWHC 756 (Ch)

Morgan J:

*In other words, instead of asking three questions, first, whether an individual is a shadow director, secondly, what fiduciary duties does a typical shadow director owe to a company and, thirdly, does the individual owe the same duties as a typical shadow director, it may be preferable to ask instead whether in all the circumstances of the case the individual owed fiduciary duties, and if so what duties, to a company.*

## (3) Consequences: Purposive Understanding

### Consequences

*Instant Access Properties Ltd (in liquidation) v Rosser and others; Murphy and another (as joint Liquidators of Instant Access Properties Ltd) v Rosser and others*

[2018] EWHC 756 (Ch)

- Shadow Director position is Problematic: What about positive duties?

Morgan J

*I referred earlier to my decision in Ross River where I held that Waveley Commercial Ltd and its director did owe fiduciary duties to Ross River but the duties which they owed were not the full fiduciary duties which would typically be owed by a trustee or a director. Accordingly, if that decision is right (and the contrary was not submitted to me), when a court is asked to determine whether a person owed fiduciary duties and the case is outside the paradigm cases where the principles are established, it is open to a court to hold that a person owed some of the usual fiduciary duties, but not all of them, or to hold that the specific fiduciary duty owed is a qualified form of the general fiduciary duty. This means that the court is not confined to an all or nothing response to the question.*

FIN



Any Questions?



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