Does a Directors’ Release Suffice to Negate Liability in Egypt?

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The Board of Directors, as commonly referred to as the ‘Board’ or individually as the ‘Directors’ as headed by a chairman, have, by law, the widest powers to run the day-to-day business affairs of the company and represent the company before third parties, including various governmental authorities, state agencies, and courts, unless otherwise restricted in the company’s statutes. Consequently, it is quite understandable that such broad powers would bring along a correspondingly equal liability exposure. Such liability can be particularly raised by the shareholders and/or the company itself.

The duties and liabilities imposed on the Directors of a joint stock company (whether such Directors are natural or juristic persons) are stipulated in several legislative sources in Egypt. The main source is the Law Concerning Joint Stock Companies, Partnerships Limited by Shares and Limited Liability Companies (Law No. 159 of 1981) and its Executive Regulations, as amended, (the “Companies Law”) in addition to some piecemeal provisions under the Commercial Code (Law No. 17 of 1999) (the “Commercial Code”), as well as the Capital Market Law (Law No. 95 of 1992) and its Executive Regulations.

Parameters and Requirements of Directorship

Basically, for a person to qualify for directorship, he cannot be convicted of a felony or misdemeanour for theft, fraud, dishonesty, forgery, bankruptcy with deceit, or any other penalty provided for under the Companies Law. The requirement not to have a criminal record is also a condition for a Director to remain in the office.

Appointing a Director, without observing the requirements set by the Companies Law, could give rise to the criminal liability of the person(s) involved in appointing such Director. Such liability further extends to the Director entrusted with the management of the company or the so called ‘Managing Director’ (i.e. the CEO).

Fiduciary Duties

Additional to the specific statutory duties and obligations of the Directors under the Companies Law and other relevant laws, the courts rely on a general concept of fiduciary duties being owed by a Director to the company and its shareholders. In that sense, a Director is assumed to owe a fiduciary duty to the company to act diligently, honestly, and in the company’s best interest.

The Egyptian State Council has issued a ruling to the effect that a Director is deemed to be an agent of the shareholders and, in this respect, he owes a fiduciary duty to the company to act honestly and avoid, unless otherwise permitted, conflict of interests. According to the Companies Law, Directors are required to inform the Board of any transaction in which they may have a conflicting interest and shall have no right to vote with respect to such matter. Furthermore, a Director must not trade for his own account, or a third party’s account, in the same branch of activities of the company without the specific permission of the general assembly of shareholders, otherwise, such transactions would be deemed to have been made in the company’s favour.

A Director's breach of his fiduciary duties would give rise to his/its liability vis-à-vis the shareholders and the company. A breaching Director who has acted to the detriment of the company would be liable to pay equitable compensation to the shareholders and the company where the latter to seek legal recourse.

Statutory Duties

The Directors of a joint stock company in Egypt are bound to run the business and affairs of the company towards achieving its object. Such management shall, in all events, be in strict compliance with the scope of their powers as determined by the Companies Law and the statutes of the company.

The Director's statutory duties are spread out under the various provisions of the Companies Law and its Executive Regulations. Some of these duties give rise to criminal liability in case of breach. By way of example, a Director would be subject to imprisonment for not less than two years and a monetary penalty of not less than two thousand Egyptian pounds and not more than ten thousand Egyptian pounds in the event that the Director, among other things, resolves on matters related to dividend distributions in a manner contradictory with the provisions of the Companies Law or the statutes of the company, or intentionally commits an act of forgery in the company's documents or otherwise presents misleading documents or falsified data to the general assembly. The sanction would be imposed personally on the perpetrating Director, if an individual, and on the corporate Director and/or its representative, in case the Director is a juristic person.

Moreover, the Director who fails to observe the parameters and scope of his directorship and powers, breaches any of the mandatory rules under the Companies Law, or intentionally obstructs the invitation of the general assembly of shareholders to convene shall be personally subject to a monetary penalty of not less than two thousand Egyptian pounds, but not exceeding ten thousand Egyptian pounds.

The aforementioned criminal liability would not prejudice third party's rights, including the shareholders and the company, to invoke the breaching Director's civil liability and claim damages remedying the losses incurred thereby due to the misconduct of such Director.

Directors' Personal Liability for Insolvent Trading

One of the significant protections invoked for the company and its shareholders, against the Directors who fail to observe their duties and conduct the business and management diligently, is the threat of rendering the Directors bankrupt upon the bankruptcy of the company. Pursuant to the Commercial Code, a Director who undertakes commercial activities for his own benefit under the company's umbrella and disposes of the company's funds and property, as if they were his own funds, may be declared bankrupt along with the company.

The Commercial Code further provides that the bankruptcy court may oblige the Directors or some of them, jointly or severally, to pay the debts of the company where the assets are insufficient to settle at least 20 per cent of such debts, unless the Directors prove that they have managed the company according to the standards of a reasonable person.

Directors' Release

According to the Companies Law, the general assembly of shareholders has to annually review the Directors' actions and decide whether to absolve the Directors of any liability resulting from their actions and management of the company during the pertinent year. In the event that the general assembly of shareholders decides to absolve the Directors, the shareholders and the company would have then waived their rights of recourse against the Directors, except in the case of a default that was then not known or disclosed to the general assembly.

Conclusion

The Directors of a company, whether natural or juristic persons, owe a fiduciary duty to such company and its shareholders and must at all times act within the scope of the powers vested therein, as well as the applicable laws and regulations. Directors’ decisions in the course of carrying out regular managerial duties shall be binding to the company vis-à-vis bona fide third parties. However, where the Directors exceed the scope of their duties or commit negligence or wilful misconduct in the course of management (as based on the actions of a reasonable person), the Directors would be liable vis-à-vis the shareholders and the company for such actions. Such liability cannot be limited or released except to the extent decided by the general assembly and provided always that the Directors’ actions do not give rise to criminal liability.