

Corporate FOCUS

06

News, views, insights & advice from
the UK's market leader.

Welcome

The Companies Act 2006 has taken over our lives at Jordans.

With many provisions affecting private companies coming into force on 1 October 2007 we have been busy amending precedents, training our staff on the changes, updating our information sheets and debating how the transitional provisions will affect existing companies.

It hasn't helped that the Government still hadn't, at the time of writing this in early September, published the final draft of the regulations amending Table A for new company formations. So, we will be finalising our M&A for company formations at the last minute, and the information in this note about Table A is based on an early draft that we saw of the regulations. If there are any changes we will let you know next time.

Having struggled ourselves to get everything in place for October 2007, I sympathise with practitioners in smaller firms who do not have professional support lawyers to help them get up to speed with the changes. If you are in this position, I hope this edition of Focus is useful. There wasn't enough room to mention every change, but we have tried to cover the key changes for private companies and the practical effect of those changes.

We are also running a number of training sessions in October for clients, and further information on these is on our Companies Act website www.companiesact.co.uk on the page entitled Jordans Seminars.

Janis Law

Janis Law Director

September 2007

Directors' duties: Are you up to speed?

As one of Jordans' Senior Legal Advisers, Philip Jacques says, "It is essential that directors are aware of these changes and also that a company's corporate practice is reviewed in light of the new provisions. Failure to do so may expose the individual and company to additional risks."

One of the more controversial parts of the 2006 Act is the codification of directors' duties. The Act will introduce a statutory statement of duties that will replace many of the existing common law and equitable duties.

The most significant changes from the 1985 Act are:

- The statutory requirement for directors to consider, amongst other things, a list of factors in exercising their duty of good faith.
- Allowing independent directors to authorise a director's conflict of interest.

The general duties of directors, which come into force on 1 October 2007, are listed below:

- A director must act in accordance with the company's constitution and must only exercise his powers for their proper purpose.
- A director must act in the way he considers, in good faith, would be most likely to promote the success of the company for

the benefit of the members as a whole. This is what has been called the principle of "enlightened shareholder value". In fulfilling this duty a director must have regard (amongst other things) to:

- (a) The likely consequences of any decision in the long-term
- (b) The interests of the company's employees
- (c) The company's relationships with suppliers, customers and others
- (d) The impact upon the environment
- (e) The company's reputation in relation to business conduct
- (f) The need to act fairly between members

This duty to promote the success of the company broadly replaces the duty of the directors to act in the best interests of the company and is the most controversial of the codified duties.

- A director must exercise independent judgement.

- A director must exercise the care, skill and diligence which would be exercised by a reasonably diligent person.
- Directors must declare to the other directors the nature and extent of any interest, direct or indirect, in a proposed transaction or arrangement with the company.

There are two additional duties – to avoid conflicts of interest and not to accept benefits from third parties – but these will not come into force until 1 October 2008. It will often be the case that more than one of these general duties will apply in any one situation. In such cases the directors must comply with each applicable duty and the duties must be read in context. So, the duty to promote the success of the company will not authorise the director to breach the duty to act within his powers, even if he considers that such a breach would promote the company's success.

Continued overleaf >>

If you want to know about how Jordans can help you implement the changes brought about by the Act, please contact Helen Goose on helen_goose@jordans.co.uk or 0117 918 1322.



JORDANS

Directors' duties: Companies Act 2006

Continued from previous page >>

There is no guidance in the Act as to the weight to be given to each of the factors and to how conflicts between duties should be resolved. As is the case under the current law, it will be up to the directors to exercise their own judgement to resolve any conflicts that may arise.

Derivative actions: Companies Act 2006

The duties of directors will continue to be owed by the directors to the company under the 2006 Act and only the company will be able to enforce them. In certain circumstances the shareholders will be able to bring a derivative action on the company's behalf.

The definition of a derivative action under the 2006 Act is made up of three parts:

- It must be brought by a member of the company.

- The cause of action must be vested in the company.
- The relief is not sought by the member on behalf of himself but on behalf of the company.

It is possible to bring a derivative claim for negligence, default, breach of duty or breach of trust by a director of the company. This means that a derivative action may be brought in respect of an alleged breach of any of the general duties of directors which were discussed above.

Directors should note that:

- There is no requirement that the director has benefited personally from the breach in order for a derivative action to be brought against him.
- There is no need for the member who wishes to bring an action to hold a specified percentage of shares – such as 5% or 10%.

- The cause of action may arise from an actual or proposed act or omission.
- There is no requirement that the shareholder held shares at the time of the alleged wrongdoing.

The legislation also provides for certain hurdles which will act as a deterrent to prevent the bringing of unjustified claims by members. For example, the shareholder is required to make a strong case for permission to continue a derivative claim. There is also the possibility that the shareholders will be responsible for the costs of an unsuccessful claim.

The court will not be able to give permission to continue a derivative claim if any person acting in accordance with the duty to promote the success of the company would not pursue the claim or the act or omission had been properly authorised or ratified.

These new provisions are unlikely to lead to US style class actions because, unlike in the US, any award for a successful claim will be made in favour of the company rather than the member.

Boards should review their liability insurance policies to ensure that their defence of any derivative actions is covered by the policies. As there is some concern that the new provisions will increase the potential exposure of directors, it may also be the case that the cost of such policies increases until it becomes clear how claims under the new law will be decided by the courts.

[If you would like further information on the changes in the Act, why not visit our website specifically set up for the Companies Act – www.companiesact.co.uk](http://www.companiesact.co.uk)

The future of the Annual General Meeting

From October 2007 private companies will no longer need to hold an Annual General Meeting in each year. This is good news for newly formed companies, but how will this provision affect the millions of existing private companies in the UK?

According to Kathleen O'Reilly, one of Jordans' Senior Legal Advisers, many private companies have already elected not to hold AGMs, and for these companies there will be no change. As now, they will continue to send copies of their accounts to their members instead of laying them before the shareholders in general meeting.

But the position is more complex for a private company which hasn't made this election. Because of the transitional provisions which apply, some companies may still have to hold an AGM.

Companies need to check the following:

- **The date of incorporation**

If the company was incorporated

before 1 July 1985 and has not updated its articles since then, it will still have to hold an AGM in each year.

This is because these companies incorporate the 1948 version of Table A in their articles, which contains an express requirement to hold an AGM.

- **Its articles of association**

The 1948 version of Table A contains an express requirement to hold an AGM, as noted above. Some companies have also written the requirement to hold an AGM into their articles, and if this has been done, an AGM must continue to be held.

Companies in this position will need to change their articles to remove these provisions if they do not want to hold an AGM.

Laying accounts

Companies that benefit from the new provisions may also find that they need to hold one more general meeting before they can stop holding annual meetings for good. This is because of the rules relating to company's accounts.

A private company must currently lay its accounts before the

members in general meeting, unless the company has elected not to do this. This is normally done at the AGM. Under the Companies Act 2006 this is replaced by an obligation to send a copy of the accounts to members. However, the new rules do not take immediate effect, and their application depends on the date to which the company's accounts are prepared:

- **Financial year ending before 1 October 2007**

The transitional provisions say that if the company's accounts relate to a financial year ending **BEFORE** 1 October 2007, the rules in the Companies Act 1985 continue to apply.

This means that the accounts must be laid before the company in general meeting. This meeting does not have to be designated as an AGM, but nevertheless a meeting of shareholders has to be held in order to receive the accounts.

- **Financial year ending on or after 1 October 2007**

The new rules in the Companies Act 2006 apply to financial years ending **ON** or **AFTER** 1 October 2007. These say that the accounts

must be sent to the shareholders instead of being laid before the shareholders in general meeting, and so a meeting is not required.

Of course, some private companies may want to continue to hold an AGM, especially if they have a large number of shareholders and the AGM is seen as a good opportunity for those shareholders to meet the board.

However, the normal business at an AGM is dealt with in a different way by the Act. As seen above, accounts are sent to members instead of being put before a meeting and auditors are deemed to be automatically reappointed. Other business, such as declaration of dividends, can be handled by written resolution. In addition, rules relating to when the AGM must be held no longer appear in the Act.

Companies that are no longer required to hold an AGM may therefore want to write into their articles an express provision which deals with such matters as when the AGM will be held and what business and resolutions will be considered at that meeting.

Meetings after 1 October 2007

The Companies Act 2006 introduces a number of changes for the conduct of meetings, which take effect in October 2007.

Lee Grove, manager of our Company Administration Department, takes a look at the effect of these changes.

When do the changes take effect?

The changes set out below apply to meetings convened on or after 1 October 2007. So, any meeting convened before this date, even if held after 1 October 2007, will apply the previous rules in the Companies Act 1985.

In addition, if the meeting is convened following a request from members to call a meeting, then the new rules only apply if the members' request was received on or after 1 October 2007.

Period of notice

The period of notice required to call a meeting is no longer dependent on the type of resolution being proposed. Instead, general meetings will be called on 14 days notice, and annual general meetings held by a public company will require 21 days' notice.

The Act confirms that clear days' notice is required, and this means that the day on which notice is given, or deemed to be given, is ignored, as is the day of the meeting itself.

The practical effect of this for most companies, where notice is deemed to be given 48 hours after serving, is that a notice posted on day 1 will be deemed served on day 3. 14 days notice ends on day 17 and then the meeting is held on day 18.

The period of notice can be extended, but not shortened, by the articles, although it is possible for members to consent to short notice.

Consent to short notice

The percentage of members required to consent to short notice is reduced to 90% (from 95%) for a general meeting held by a private company and remains at 95% for a general meeting held by a public company.

A public company may hold an AGM on short notice if all members so agree.

Form of the notice

The form of the proxy statement on the notice will change, because the Act requires the company to state, with reasonable prominence the member's rights under CA06, s324 i.e. that:

- (a) the member is entitled to appoint another person as his proxy to exercise all or any of his rights to attend, speak and vote at a meeting of the company; and
- (b) a member of a company limited by shares may appoint more than one proxy provided that each proxy is appointed to exercise the rights attached to a different share or shares held by him

and to contain a statement of any more extensive rights to appoint more than one proxy conferred by the company's articles.

In addition, if the company includes an electronic address on the notice – such as an email or fax address – it will be deemed to have consented to members sending documents which relate to the meeting to the company by that means.

Proxies

Proxies are given new rights to both speak and vote on a show of hands at the general meeting. Previously this was only permitted if the company's articles so provided.

Proxies may also be appointed by a guarantee company.

As seen above, a proxy of a company limited by shares may also appoint more than one proxy, as

long as each proxy is appointed to exercise the rights attaching to different shares.

The Act also provides that when calculating the period of time by which the proxy must be received by the company, only working days are counted. This is a change to the previous law where the date for receipt of a proxy form could have been a Saturday or a Sunday.

Corporate representatives

Corporate members may still appoint representatives to attend meetings. Their rights are extended so a corporate member can appoint more than one representative, but if this is done and the representatives all attend the meeting and try to vote in different ways, none of the votes are counted. So, if a corporate representative wishes to vote its shares in different ways, it will either have to appoint one representative or multiple proxies.

Requisition of meetings by members

The percentage of members who may require a meeting to be held is reduced from members holding 10% of the paid up share capital to members holding 5% if a general meeting has not been called by the members within the previous 12 months.

Other changes in October 2007

- Filing resolutions at Companies House – s30 replaces s380, CA85 but makes no major changes.
- Removal of a director – s168 replaces s303, CA85. No major changes other than clarification that the resolution is passed at a meeting.
- Directors' long term service contracts require member approval if the guaranteed term is, or may be, longer than two years, reduced from five years under the CA85. This applies to agreements made on or after 1 October 2007.
- Substantial property transactions – s190 replaces s320, CA85. Members' approval is still required to a substantial property transaction between the company and its director. The only change is the valuation of a substantial asset – it must have a value in excess of 10% of the company's net assets and more than £5000 or it must have a value in excess of £100,000.
- A company may ratify any negligence, default, breach of duty or breach of trust by a director occurring on or after 1 October 2007 by ordinary resolution – s239.
- From 1 October 2007, the only elective resolution which will be available to be passed is that under s80A, CA85, which amends the company's authority to issue shares. The others are repealed. There is one exception to this. Under the transitional provisions, existing companies may continue to pass an elective resolution to dispense with laying accounts before a general meeting in relation to financial periods ending before 1 October 2007.
- The extraordinary resolution disappears. Statutes now refer to 'special resolutions' instead of extraordinary resolutions. However, any references to extraordinary resolutions in private documents will be interpreted in accordance with s378, CA85.

Reminder

The transitional provisions preserve the old rules in the Companies Act 1985 for the holding of shareholder meetings and the passing of resolutions if the notice of the meeting was sent out on or before 1 October 2007. So, even if the meeting is held or the resolution is signed after 1 October 2007 the old rules will continue to apply.

Articles of Association on or after 1 October 2007

On 1 October 2007 The Companies (Tables A to F) (Amendment) Regulations 2007 will amend Table A. Table A sets out the articles which apply to companies limited by shares by default if they fail to file articles on incorporation. It is incorporated into most company's articles.

The approach taken by the Government in updating Table A is to omit any provision which may be inconsistent with the provisions of the Companies Act 2006 ("the Act") which will come into force on 1 October 2007.

The key changes are:

- There will be two versions of Table A – one for private and one for public companies.
- A new definition of "the Acts" to include both the 1985 and 2006 Companies Acts.
- For a private company only, the deletion of regulation 36, which requires any general meeting other than an AGM to be called an "extraordinary" general meeting. As a result, new companies will hold general meetings, not EGMs, in line with the Act.
- The deletion from regulation 38 of the requirement for 21 days' notice if a special resolution is passed, as the notice period for meetings in the Act is not dependent on the type of resolution being passed.
- Regulation 53 – resolutions in writing – is deleted for both public and private companies.

Only private companies may pass written resolutions under the new procedure in the Act.

- All references to AGMs are deleted in the version for private companies, together with the director retirement by rotation provisions in regulations 73 to 75.
- The reference in regulation 117 to an extraordinary resolution for winding up is replaced by a special resolution.

These new versions of Table A only apply to companies incorporated on or after 1 October 2007, and in October 2008 will be replaced by the new model form articles.

Existing companies should review their articles to check that the version of Table A which applies to them does not prevent them from benefiting from the deregulatory provisions introduced in October.

There are two main points to note:

- A private company with 1948 Table A will be required to hold an AGM.
- A private company which incorporates regulation 38 will need to give 21 days' notice of the passing of a special resolution at a general meeting instead of the 14 days required by the Act, as this provision in its articles will override the Act.

Companies in these situations may wish to amend their articles to remove the offending provisions. Contact Helen Goose for assistance with this.

Access to register of members

One of the changes this October makes it harder to get information on the members of the company.

It has always been the case that any person may inspect and copy the register of members on payment of a fee, and this remains the position.

However, after 1 October 2007 companies are given power to apply to court to prevent access to the register.

The new provisions apply if:

- a person asks to see the register on or after 1 October 2007; and
- the company is not obliged to deliver an annual return made up to a date before October 2008.

The request must be made in a specific form – and in particular it must set out who is making the request and the purpose for which the information that they get from the register is to be used.

The company, within 5 working days of receiving the request, must either

provide access or apply to the court for an order that it does not need to comply with the request. The order will be made if the court believes that access is not sought for a proper purpose. What is a proper purpose is not described in the section, so the courts will decide this on the merits of the case.

If the court makes the order, it can also order that the costs of the court application be borne by the person seeking access.

It is hoped that these provisions will prevent pressure groups obtaining access to the names and addresses of company members for improper purposes.

This protection only applies to a company whose last annual return is dated on or after 1 October 2007.

Companies can therefore get the protection of this section for their members by bringing forward the filing of their next annual return.

Clients of our company administration department should contact their administrator if they wish to do this.

For further information on the changes in the Act why not visit our website specifically set up for the Companies Act – www.companiesact.co.uk or if you want to know about how Jordans can help you implement these changes please contact Helen Goose on helen_goose@jordans.co.uk or 0117 918 1322.