

Collins**B**enson**G**oldhill Legal Briefing

PRIVATE LIMITED COMPANIES CHANGES UNDER THE COMPANIES ACT 2006



BE PROACTIVE

Companies Act 2006

Now that the Companies Act 2006 ("the Act") has been fully implemented (as of 1 October 2009) it is time for companies to assimilate the changes that have been made to company law and to take full advantage of the new statutory provisions which aim to bring the law in line with modern technology.

ELECTRONIC COMMUNICATIONS WITH SHAREHOLDERS

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- Review your company's website. A company's website must state its name, registered number, place of registration and registered office address (this requirement also applies to a company's order forms).
- If you would like to have an agreement in place with your company's shareholders to allow you to supply them with documents in electronic format, please contact us for advice.
- In addition you should review your business letters and order forms etc and make sure that they all display your company's place of registration, company number and registered office.
- If your company's business letters list directors of your company then it must list all of the directors or none at all to ensure compliance with the Act.

The Act has recognised the changes that have occurred in modern technology and the way in which people communicate with one another by acknowledging the increasing importance of electronic communications in the business community.

Schedule 5 of the Act includes provisions permitting a company to

- keep records in electronic form (provided it can be printed out if required) and that directors take active steps to protect some records from falsification (s.1138 of the Act);
- communicate by email or other electronic method (for example a chat room) with a person by agreement; and
- publish documents or information on its website subject to members' approval.

There are of course exceptions to the above but in general the Act seeks to make plain the rules surrounding email and other web based communications.

If you have any questions regarding this article or would like to know more about a specific area regarding the Companies Act 2006, then please feel free to contact a member of our Business Services Team:

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COMPANY CONSTITUTIONAL MATTERS

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- Review your articles and bear in mind the pointers above; can your company take advantage of the changes in company law permitted by the 2006 Act?
- If incorporating a new company will the Model Articles be appropriate for your specific circumstances?
- Do you need to entrench any provisions in the Articles in order, for example, to retain control or position on the Board?

Articles of Association

Existing companies incorporated under the Companies Act 1985

There is no immediate requirement to adopt new articles of association to replace your existing articles. The Act provides that existing articles can continue without amendment but please read on for potential reasons why you might choose to. If any provision in your existing articles ever conflicts with a provision of the new Act then it will not be enforceable. As of 1 October 2009 the company's name, the location of the company's registered office, the company's objects, the statement that the liability of the members is limited and the statement regarding the company's share capital will all be deemed to be part of the company's articles of association.

New companies incorporated under the Companies Act 2006

For new companies incorporated under the Companies Act 2006, the articles of association will be the main constitutional document containing restrictions on a company's objects (if any) under the Act. Shareholders' rights will also be set out in the articles (supplemented by a shareholders' agreement where necessary). The memorandum of association merely sets out who the subscriber shareholders will be and that they agree to become members of the company, with at least one share each. After incorporation the memorandum is of no ongoing relevance.

Entrenchment

The term "provision for entrenchment" is defined in section 22(1) of the 2006 Act as a provision contained in a company's articles the effect of which is "that specified provisions of the articles may be

amended or repealed only if conditions are met, or procedures are complied with, that are more restrictive than those applicable in the case of a special resolution”.

Before 1 October 2009, provisions could be entrenched by including them in the memorandum of association and prohibiting their amendment. Any entrenched provisions contained in a memorandum of association immediately before 1 October 2009 will now be treated as provisions of the articles.

However, the effect of s.22(3)(a) of the 2006 Act is that provisions can no longer be entrenched absolutely; the entrenched provisions can always be amended if the amendments are unanimously approved by all shareholders entitled to vote. Transitional provisions provide that this does not apply to entrenched provisions if they could not be amended by unanimous shareholder approval immediately before 1 October 2009.

Section 24 of the 2006 Act has introduced a new obligation for companies to file a statement of compliance whenever they amend their articles – this certifies that the amendments made to the articles have been made in accordance with the provisions of the existing articles.

Model Articles

Under section 19 of the 2006 Act, the Secretary of State has been given the power to prescribe model articles of association for different types of company. The form of the model articles is in the Companies (Model Articles) Regulations 2008 (SI 2008/3329) and as of 1 October 2009 they have replaced Table A as the default set of articles for limited companies incorporated on or after that date.

You should note that the model articles automatically apply to companies that choose not to modify or exclude the provisions of the relevant model in its registered articles.

Whatever the form of company's articles, their contents will be subject to, amongst other things, the provisions of the 2006 Act. Generally the 2006 Act overrules the articles, but it also recognises that not all of its provisions will be suitable for companies, and so, in a number of places, it allows a company to include vary or exclude, certain of its provisions.

The provisions of the 2006 Act contain a number of changes from the 1985 Act relating to a company's articles of association (articles). Companies should now BE **PROACTIVE** and review their articles to consider whether to change the articles to:

- Take advantage of the new provisions of the 2006 Act.
- Ensure that the implementation of the 1 October 2009 changes does not affect the operation or validity of any existing provisions of its articles.
- Eliminate redundant provisions and out of date references to sections of the 1985 Act.
- Remove unnecessary restrictions and obligations.

The following are issues you may wish to consider when reviewing your existing articles

CONSTITUTION

- Should the company update its articles and, if so, will the company keep Table A or adopt the Model Articles as the default set of articles?
- Do the company's articles, or its memorandum, contain or need any entrenched provisions which may only be amended in accordance with procedures or conditions more stringent than those required to pass a special resolution? If so, are they still relevant to the company?
- Does the memorandum set out specific objects of the company and, if so, should they remain?
- Do the articles (or the memorandum) contain any provision for the appointment of any person as attorney of a member?

ISSUES OF SHARES

- Does the company have only one class of shares (or do the articles contain any mechanism by which the company may, at some future point, have only one class of shares)? If so, should the directors have power to allot further shares of that single class without the need for further shareholder approval (as is now permitted)?
- Where the company has only one class of shares and the directors are authorised to allot shares under section 550 of the 2006 Act, should the directors also have power to allot shares without observing the statutory pre-emption procedure?
- Will the company retain the current statement of the authorised share capital (as this is no longer a requirement under the 2006 Act)?
- Do the company's articles (or any elective resolution) grant an indefinite (or extended) authority to allot shares pursuant to an elective resolution under section 80A of the 1985 Act? If not, would the company consider it advantageous to have such an indefinite (or extended) authority in place?

ALTERATION OF SHARE CAPITAL

- Does the company wish to restrict a sub-division or consolidation of its shares?
- Does the company wish to restrict a redenomination into other currencies of any of its share capital?

REDEMPTION AND PURCHASE OF OWN SHARES

- Does the company wish to restrict its ability to issue redeemable shares?
- Should the company's directors be able to determine the terms, conditions and manner of redemption of any redeemable shares?
- Does the company want flexibility as to the timing of payment for any redemption of redeemable shares?
- Does the company wish to restrict its ability to purchase its own shares?
- Does the company want to be able to fund a purchase of its own shares from capital?

COMPANY NAMES

- Does the company wish to have flexibility to change its name without need for a special resolution of the shareholders?

PROVISION FOR EMPLOYEES ON CESSATION OF TRANSFER OF BUSINESS

- Do the company's articles permit the directors to make provision for the directors, former directors or shadow directors of any group company on the cessation of that group company's business or its transfer (whether in whole or in part) to any person?

As you can see there are a number of areas in which a company can amend their articles to make the day to day running of their business easier and potentially more efficient. If there are any aspects above which are of interest to you and you would like to know more then please contact a member of our team to discuss further.

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MEETINGS AND MAKING DECISIONS

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- If you need advice on how to take advantage of the new legislation regarding written resolutions or the necessary information to make them compliant with the 2006 Act please contact us.
- If your private company want to do away with the formality of holding an AGM, review your articles to make sure it is not an express requirement.

Annual General Meeting

One of the main objectives of the Act is to make life easier for private companies.

Now only public companies and private companies that are listed are required to hold an AGM under the 2006 Act.

Private companies are no longer required to hold AGM's, although they may decide to continue to do so for reasons of good governance. Now only 14 days notice are required for such a private company's AGM.

A provision specifying that one or more directors are to retire at an AGM does not count as a provision expressly requiring a non-traded private company to hold an AGM.

Please take note that private companies are not obliged to lay accounts and reports before general meetings. Therefore, for private companies there is no longer a statutory link between the accounts and AGMs, although the articles may create such a link.

Written Resolutions

Under the 2006 Act only private companies can pass written resolutions.

Written resolutions can be passed with the requisite number of votes for an ordinary (simple majority) or special resolution (75%) as opposed to unanimity.

Procedural details covering the circulation of, and timing for the passing of, written resolutions are included in the 2006 Act in much greater detail than was the case in the 1985 Act:

- the copy of the written resolution must be accompanied by a statement informing the members how to signify agreement to the resolution and the date on which the resolution must be passed if it is not to lapse (please see refer to your articles for the minimum period)

- members who are eligible to vote on written resolutions are those members entitled to vote on the circulation date of the resolution (as opposed to members entitled to vote at the date of the resolution pursuant to the 1985 Act).
- for a written resolution to be passed as a special resolution it must be expressly stated as such.
- once a member has signified his agreement to a written resolution, his agreement may not be revoked

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ACCOUNTS

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- Note that company accounts must be filed more quickly. Nine months after year end for private companies and six months for Plc's.
- Note that abbreviated accounts are acceptable for "larger" small companies.

The provisions of the Act relating to accounts and reports were implemented in full but please note that they only apply to financial years commencing on or after 6 April 2008.

The delivery time for accounts has been reduced by one month (i.e. private companies must file accounts within nine months of the end of the accounting reference period and public companies within 6 months). The reduction in the time for filing is mitigated by the introduction of full calendar month filing periods. Therefore, if the accounting period ends on the last day of the month then the filing period also ends on the last day of the relevant month.

Although **abbreviated** accounts can still be filed, the qualifying annual turnover and balance sheet thresholds for a small company have been increased to £6.5m and £3.26 respectively and for a medium sized company to £25.9 and £12.9m.

The accounts must show a "true and fair" view of the financial position of the company if the directors are to approve them.

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REDUCTION OF SHARE CAPITAL

A private company may now reduce its share capital without making an application to court. A company now has the option of reducing the amount of their share capital by special resolution supported by a solvency statement signed by all of the directors. It is a criminal offence, however, for a director to sign a solvency statement without having reasonable grounds to support it. If one or more directors refuses to sign the solvency statement then the company must pursue the application to court route.

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- If you are considering making a reduction in share capital but are not sure how the amendments made by the 2006 Act have altered the way you can do this then contact our Business Services Team for more advice.
- Note less restrictive regime for buyers to use company assets to finance their acquisition of shares

OBJECTING TO A COMPANY'S NAME

As of 1 October 2007 new rules came into effect which allow complaints to be made where a company has been registered with the intention of extracting money from the complainant or to prevent him from registering a name in which he has goodwill ("opportunistic registration"). All objections about opportunistic registration must be sent to the new and independent Company Names Tribunal which is based at the UK Intellectual Property Office. If an objection is upheld then the complainant can stop the offending name from being used before that company starts trading.

WHITEWASH PROCEDURE – REMOVED FROM ACT

To the joy of many company directors, the Act has removed the general prohibition on financial assistance by private companies for the acquisition of shares in itself or in other private companies. Accordingly, the "whitewash" procedure (as it was known under the Companies Act 1985) will no longer be necessary for private companies.

Please note however that Plc's remain bound by financial assistance rules.

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COMPANY DIRECTORS and COMPANY SECRETARIES

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- Review your duties as a director and ensure that your board practices are in alignment with the new codified law.
- Review your articles to see what they say in regard to indemnification of its directors
- Do your directors have indemnity policy's in place, and if not, do they want them, bearing in mind the new codification of duties?
- Does your company have insurance policies in place for its directors? If not, why not?
- Are you a private company with only corporate directors, if so you will need to appoint at least one new "natural" director before 1 October 2010.
- Check your articles to see whether you need a company secretary. If they do but you want to dispense with the role then contact us for advice on changing your articles.
- If you are not sure whether you or someone you have entered into a contract or deed with has executed the document correctly please call Collins Benson Goldhill LLP for verification.
- Make a decision whether or not you want to have a casting vote and then check to see your articles reflect your preferred position.

Codification of Directors Duties

If you are a company director (or for that matter a shareholder) you should pay particular attention to the new codification of directors' duties that the Act has brought in. These changes are a codification and extension of the common law and equitable duties of directors. In summary, the seven general duties under the 2006 Act are:

- To act within powers.
- To promote the success of the company.
- To exercise independent judgment.

- To exercise reasonable care, skill and diligence.
- To avoid conflicts of interest.
- Not to accept benefits from third parties.
- To declare an interest in a proposed transaction or arrangement.

The full Companies Act 2006 provisions can be found by clicking on this link [INSERT LINK]. Please be aware however that the codification is not exhaustive, and directors will still have certain duties under common law and equity. The previous law on directors' duties will therefore remain highly relevant.

Action by the company

The codified duties are owed to the company and only the company will be able to enforce them, although in certain circumstances shareholders may be able to bring a derivative action on the company's behalf (please see our note on Derivative Actions for further details).

Indemnity and insurance

Under section 232 of the 2006 Act, a company will not be able to exempt a director from any liability for negligence, default, breach of duty or breach of trust in relation to the company.

The company may, however, indemnify the director against defence costs, or costs incurred in an application for relief under section 1157 (above), provided that the director repays the costs if he is unsuccessful.

Section 232 of the 2006 Act will not prevent a company's articles including provisions that have previously been lawful for dealing with conflicts of interest

Section 233 of the 2006 Act permits a company to purchase insurance for its directors, and those of an associated company, against any liability attaching to them in connection with any negligence, default, breach of duty or breach of trust by them in relation to the company of which they are a director

“Corporate” Company Directors

The Act requires that all private companies must have at least one director and all public companies must have at least two directors. All companies must now have at least one director who is a natural person (i.e. not a corporate body). The transitional period for implementing these changes come to an end on 1 October 2010, so BE PRO**ACTIVE**!

Any newly appointed directors have to be over the age of 16 and any directors under the age of 16 will automatically cease to be a director.

New business review reporting provisions for directors are being implemented for all but the smallest private companies, tying in with the duty to show that they are acting to promote the success of the company.

Company Secretary

A private company is no longer required to have a company secretary. Instead a director (or another person authorised by the directors) can undertake their duties. However, if a company's articles state that it is required to have a secretary then it must have one or amend its articles to dispense with the role.

Executing Deeds

Following full implementation of the Act there are now three methods for a company to execute a deed:

- 1) by company seal;

- 2) by two company officer; or
- 3) by one director in the presence of a witness

The rules for signing a simple contract remain the same (i.e. by seal or an authorised signatory).

Chairman's casting vote

If you have a chairman's casting vote provision in your articles then this will continue to operate on the same basis. However, the use of such a provision in a company's articles has been made void by the Act for new companies. If a company has removed the casting vote provision from its articles since 1 October 2007 then it may reinstate it should want to.

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COMPANIES ACT 2006 – DIRECTORS DUTIES**171 Duty to act within powers**

A director of a company must—

- (a) act in accordance with the company's constitution, and
- (b) only exercise powers for the purposes for which they are conferred.

172 Duty to promote the success of the company

(1) A director of a company 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 its members as a whole, and in doing so have regard (amongst other matters) to—

- (a) the likely consequences of any decision in the long term,
- (b) the interests of the company's employees,
- (c) the need to foster the company's business relationships with suppliers, customers and others,
- (d) the impact of the company's operations on the community and the environment,
- (e) the desirability of the company maintaining a reputation for high standards of business conduct, and
- (f) the need to act fairly as between members of the company.

(2) Where or to the extent that the purposes of the company consist of or include purposes other than the benefit of its members, subsection (1) has effect as if the reference to promoting the success of the company for the benefit of its members were to achieving those purposes.

(3) The duty imposed by this section has effect subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company.

173 Duty to exercise independent judgment

(1) A director of a company must exercise independent judgment.

(2) This duty is not infringed by his acting—

- (a) in accordance with an agreement duly entered into by the company that restricts the future exercise of discretion by its directors, or
- (b) in a way authorised by the company's constitution.

174 Duty to exercise reasonable care, skill and diligence

(1) A director of a company must exercise reasonable care, skill and diligence.

(2) This means the care, skill and diligence that would be exercised by a reasonably diligent person with—

- (a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company, and
- (b) the general knowledge, skill and experience that the director has.

175 Duty to avoid conflicts of interest

(1) A director of a company must avoid a situation in which he has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company.

(2) This applies in particular to the exploitation of any property, information or opportunity (and it is immaterial whether the company could take advantage of the property, information or opportunity).

(3) This duty does not apply to a conflict of interest arising in relation to a transaction or arrangement with the company.

(4) This duty is not infringed—

- (a) if the situation cannot reasonably be regarded as likely to give rise to a conflict of interest; or
- (b) if the matter has been authorised by the directors.

(5) Authorisation may be given by the directors—

- (a) where the company is a private company and nothing in the company's constitution invalidates such authorisation, by the matter being proposed to and authorised by the directors; or

(b) where the company is a public company and its constitution includes provision enabling the directors to authorise the matter, by the matter being proposed to and authorised by them in accordance with the constitution.

(6) The authorisation is effective only if—

- (a) any requirement as to the quorum at the meeting at which the matter is considered is met without counting the director in question or any other interested director, and
- (b) the matter was agreed to without their voting or would have been agreed to if their votes had not been counted.

(7) Any reference in this section to a conflict of interest includes a conflict of interest and duty and a conflict of duties.

176 Duty not to accept benefits from third parties

(1) A director of a company must not accept a benefit from a third party conferred by reason of—

- (a) his being a director, or
- (b) his doing (or not doing) anything as director.

(2) A "third party" means a person other than the company, an associated body corporate or a person acting on behalf of the company or an associated body corporate.

(3) Benefits received by a director from a person by whom his services (as a director or otherwise) are provided to the company are not regarded as conferred by a third party.

(4) This duty is not infringed if the acceptance of the benefit cannot reasonably be regarded as likely to give rise to a conflict of interest.

(5) Any reference in this section to a conflict of interest includes a conflict of interest and duty and a conflict of duties.

177 Duty to declare interest in proposed transaction or arrangement

(1) If a director of a company is in any way, directly or indirectly, interested in a proposed transaction or arrangement with the company, he must declare the nature and extent of that interest to the other directors.

(2) The declaration may (but need not) be made—

- (a) at a meeting of the directors, or
- (b) by notice to the directors in accordance with—
 - (i) section 184 (notice in writing), or
 - (ii) section 185 (general notice).

(3) If a declaration of interest under this section proves to be, or becomes, inaccurate or incomplete, a further declaration must be made.

(4) Any declaration required by this section must be made before the company enters into the transaction or arrangement.

(5) This section does not require a declaration of an interest of which the director is not aware or where the director is not aware of the transaction or arrangement in question.

For this purpose a director is treated as being aware of matters of which he ought reasonably to be aware.

(6) A director need not declare an interest—

- (a) if it cannot reasonably be regarded as likely to give rise to a conflict of interest;
- (b) if, or to the extent that, the other directors are already aware of it (and for this purpose the other directors are treated as aware of anything of which they ought reasonably to be aware); or
- (c) if, or to the extent that, it concerns terms of his service contract that have been or are to be considered—

- (i) by a meeting of the directors, or
- (ii) by a committee of the directors appointed for the purpose under the company's constitution

