

UK – Law Firms

Company Law Reform Bill

By Adam Dowdney
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Introduction

The UK's existing company legislation is based on a 19th Century vision of a large corporation where management is divorced from ownership. This Victorian perspective is increasingly irrelevant to the majority of UK companies in the 21st Century. To address this the Government has undertaken seven years of review and consultation and this has resulted in the new Company Law Reform Bill finally making its way to the House of Lords in November 2005. However, the new Company Law Reform Act is not expected to come into force until late 2006 or early 2007. It is the Government's intention that the Bill will:

- Enhance shareholder engagement and encourage a long-term investment culture.
- Ensure better regulation and a "think small first" approach.
- Make it easier to set up and run a small company.
- Provide better flexibility for the future.

The Bill aims to simplify and modernise the existing rules and to clarify (and codify) the position of directors. Some of the key proposals are detailed below. It is important to note that the Bill amends some of the provisions on the Companies Act 1985 but does not replace this Act; the two acts will sit alongside each other.

Adam Dowdney is Head of the Corporate Department in the London office of Clarkslegal LLP. Clarkslegal LLP is a leading commercial law firm with a proven track record across the UK and internationally. With offices in the Thames Valley, London and Cardiff, Clarkslegal LLP is also a member of TAGLaw, a worldwide legal network of independent law firms. The TAGLaw network has 134 firms in 80 countries and 120 jurisdictions. After six years of operation, the network has grown substantially and is today one of the largest in the world in terms of the number of countries and jurisdictions covered. The network permits its members to draw upon the expertise and connections of law firms that are well established in their jurisdictions and, in particular, on the experience of lawyers who have a great deal of familiarity with their own communities and with the conduct of business there. This is an invaluable resource in a number of areas but particularly important in the resolution of issues relating to the employment of people in other countries. Clarkslegal LLP has also been active in providing legal advice and support to the British employers' delegation to the International Labor Organization's annual conference in Geneva. Visit the website of Clarkslegal LLP at www.clarkslegal.com.



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Key Changes

1. Directors

The general duties owed by directors to their company will be set out in statutory code. Most of the directors' duties have already been established by common law, however, additional changes will be introduced and, in par-

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ticular, in relation to avoiding conflicts of interests.

- There will be a statutory duty on directors not to accept benefits from third parties unless the benefit cannot reasonably be regarded as likely to give rise to a conflict of interests.

- Directors will be required to exercise the same level of skill, care and diligence as they would in carrying out any other task, at least as far as is "practically possible" in the particular circumstances; however, these duties are not particularly onerous and will probably be easily fulfilled if directors can show that they at least considered them.

- The Bill will maintain the existing position that the core directors' duties are owed to, and are therefore only enforceable by or on behalf of, the company and also confirm that a breach of such duties may be authorised or certified by an ordinary resolution of shareholders (excluding the votes of the directors in question). Currently, a shareholder can only bring a claim on behalf of a company for breach of duties owed to the company if he can show "fraud on the minority." The Bill proposes that shareholders have a general right to bring a claim for

breach of duty (which has not been authorised or ratified by the company) but the claim will be on behalf of the company with all proceeds going to the company and the court's permission will be required to bring the claim.

- All companies will be able to make loans to their directors provided these are approved by shareholders. The rules on quasi-loans and credit transactions that currently only apply to public companies will be widened to also cover private companies.

- Shareholders' approval will be required where a company proposes to make a final termination payment to a director in compensation for loss of employment.

- Transactions with third parties (ultra vires) will be deemed to be unrestricted as far as third parties are concerned and, as long as they are not prohibited by the company's own articles of association.

- There will be new rules allowing for a director's residential address to be excluded from the register of companies. However, existing residential addresses on the register will not be removed.

- It will be possible for a public company to have one director only while private companies will no longer

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need to have a company secretary.

- Directors will be subject to a duty not to approve accounts unless they are satisfied that they give a true and fair view of the assets, liabilities, financial position and profit and loss of the company.

2. Capital maintenance and shareholders transactions

- Private companies will no longer be required to go through the "white-wash" procedure before being able to give financial assistance for the acquisition of their own shares or those of their (private company) parent. This should reduce professional costs and assist in the sale or purchase of private companies. It is expected that few will object to this amendment.

- Private companies will be able to reduce their share capital by passing a special resolution, supported by a directors' solvency statement signed by all directors as opposed to going through the court as the current position stands.

- The concept of an authorised share capital will be abolished. The requirement for the issue of shares to

be approved (generally or specifically) will largely remain, as will the right to participate pre-emptively in cash offers of shares.

3. Auditors and accounts

- There will be a new criminal offence of knowingly or recklessly giving an incorrect audit opinion.

- Companies and auditors will be permitted to agree to a cap on auditors' liability to the company subject to annual shareholder approval. But if the court, in respect of a particular claim, thinks the cap is not fair and reasonable, the amount recoverable will be what is fair and reasonable rather than the cap. Such a limitation agreement must be disclosed in a company's annual financial statement.

- Private companies will have to file annual reports and accounts at Companies House within seven months of their year end (currently ten months) and public companies within six months (currently seven months).

4. Company administration

- Private companies will not be required to lay their accounts or to appoint an auditor (if they have one) at an AGM. Holding an AGM will also become an "opt-in" regime.

- Members of both public and private companies will be able to appoint more than one proxy. Proxies will be given the same rights as registered holders to ask questions, demand a poll and vote.

- The ability to pass shareholder resolutions by way of written resolutions is to be enhanced by reducing the required percentages of signatories to those applicable to the resolution in question (50% for ordinary and 75% for special resolutions). The written resolution procedure will not be extended to public companies.

- Subject to shareholder approval, companies will be able to make electronic communications to shareholders.

- There will be some changes to the rules on political donations, which may mean changes to the number and wording of resolutions presented to shareholders.

- The notice period required for meetings will be standardised at 14 days regardless of the type of resolution to be proposed (except for public company AGMs where the notice period will remain at 21 days).

- The core of the recent EU Takeover Directive will also be implemented in the UK through this Bill.

Summary

Although promising much, the Bill does not go as far down the road of reform as many expected and perhaps hoped. It will be interesting to see how the Bill is received generally and in what shape it is when it is passed, which is expected to be in the summer of 2006 with the majority of its provisions coming into force in April 2007.

Please email the author at adowdney@clarkslegal.com with questions about this article.