



COMPANY LAW MEMO 2007

Newsletter Issue 1

March 2007

▶ **Contents**

▶ **News**

▶ **Cases**

▶ **Legislation**

▶ **Focus on...**

▶ **CA 2006**

▷ **All newsletters**

▷ **Online updates**

▷ **Email us**



PDF printer
friendly version

Welcome to the *Company Law Memo 2007* newsletter, highlighting important recent developments in company and insolvency law. You can also access comprehensive updates to specific paragraphs via our online updating service. We always welcome suggestions from readers, so please contact us if you have any comments.

In this issue...

Shares and share capital:

- » DTI consultation on EC Directive on capital maintenance and share capital

Directors:

- » Director's breach of fiduciary duties

Company accounts:

- » DTI consultation on EC Directive on company reporting
- » DTI consultation on EC Directive on statutory audit

Corporate transactions:

- » Budget 2007
- » Payment of fee to introducing agent not financial assistance
- » Meaning of "reasonable endeavours"
- » FAQ on Prospectus Directive
- » Takeover Panel publishes amendments to City Code
- » DTI consultation on EC Directive on cross-border mergers

Litigation:

- » *Focus on...*The Corporate Manslaughter Bill

Insolvency:

- » Winding up petition deposit increase
- » Insolvency Service's review of secondary legislation
- » Effect of EA 2002 on realisations and costs
- » Can rates be paid as an expense of administration?

Companies Act 2006:

- » Implementation timetable
- » DTI consultation on secondary legislation and transitional arrangements

Disclaimer

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NEWS ROUND-UP

Budget announcements

The Budget on 21 March 2007 threw up a few surprises, most notably the cut in the basic rate of income tax which will apply from 6 April 2008.

For **full details** on all the budget announcements, see *Tax Memo 2006/07 Newsletter Issue 4*.

You can access **specific changes** to particular paragraphs in *Company Law Memo 2007* through the online update service.

FAQ on Prospectus Directive

See CLM: ¶¶4845

The Committee of European Securities Regulators (CESR) has published answers to frequently asked questions on the Prospectus Directive.

The FAQ document can be downloaded from the CESR's website (www.cesr-eu.org).

Takeover Panel publishes amendments to City Code

See CLM: ¶¶6688, ¶¶6700+

On 7 March 2007, the Takeover Panel published the changes which it will be making to the City Code as a result of Part 28 of the Companies Act 2006 coming into force. These changes, like Part 28, will come into effect on 6 April 2007.

Many changes are simply a substitution of a reference to the Companies Act 2006 for the old reference. However, the substantive changes set out below will be made.

- » **Transitional arrangements** will make it clear that the Panel can exercise its statutory powers in relation to all bids which are covered by the amended Code which started before 6 April 2007 and any breaches which occurred or rulings which were given before that date (Intro para 2(d) City Code).
- » The Code will not have statutory effect for takeovers of companies in the **Channel Islands** or the **Isle of Man** (unless and until legislation to that effect is passed, either by secondary legislation in the UK or local legislation in those jurisdictions). The Code will continue to apply to those companies, as it does now, but the Panel will not be able to exercise any of its statutory powers (Intro paras 1, 2(a) City Code).
- » A footnote will be added to clarify that, in the case of an **unregistered company** with a principal office in the UK, the term "registered office" should be read as a reference to its principal office (Intro paras 3(a) City Code).
- » It will be clarified that the **overriding principle for determining jurisdiction** over an offer is that if the target has securities admitted to trading on a regulated market in the same member state in which it has its registered office, then the regulator of that member state has sole jurisdiction over the offer (Intro para 3(a)(iii)(C) City Code).
- » Changes to **regulatory references** to reflect the fact that certain provisions of the Companies Act 1985 have been repealed and partly replaced by provisions in the Companies Act 2006 and partly by Chapter 5 of the FSA's Disclosure and Transparency Rules.
- » The **directors' interests in shares** to be disclosed by the bidder in the offer document will be determined by reference to Part 22 of the Companies Act 2006 (ss 792, 820-825 CA 2006) not the Companies Act 1985 provisions, which will be repealed from 6 April 2007; and
- » Changes to reflect the **change of name of OFEX** to PLUS Markets Group.

- ▶ Contents
- ▶ News
- ▶ Cases
- ▶ Legislation
- ▶ Focus on...
- ▶ CA 2006

- ▶ All newsletters
- ▶ Online updates
- ▶ Email us



PDF printer friendly version

News



NEWS ROUND-UP cont...

Insolvency Service's review of secondary legislation

See CLM: ¶7364

The Insolvency Service has announced that its review of secondary legislation is moving to the next stage. It will send 20 draft Parts of the new Insolvency Rules to selected stakeholders for consultation by the end of this month and expects to be able to submit a full draft of the new Rules to the Insolvency Rules committee in June.

The Insolvency Service's plans for revising and updating the Rules were discussed in *Company Law Memo 2006 Newsletter Issue 5*.

The effect of the Enterprise Act 2002 on realisations and costs

See CLM: ¶8691, ¶8692

The Insolvency Service has published a **report** into "The Impact of the Enterprise Act 2002 on Realisations and Costs in Corporate Rescue Proceedings" (by John Armour, Audrey Hsu and Adrian Walters). It analyses statistical data and opinions gathered from insolvency practitioners and others in the corporate recovery profession to compare and contrast pre-Enterprise Act administrative receiverships and post-Enterprise Act administrations.

The report highlights several **key findings**:

- » even though holders of pre-Enterprise Act floating charges can still appoint administrative receivers, the number of administrator appointments has increased significantly and the number of administrative receiver appointments has decreased. The interview evidence suggested that this was largely due to banks favouring administrations, unless they are under-secured and there is therefore no chance of other creditors making a recovery, or unless a receivership would result in tax savings;
- » administrations see higher gross recoveries than administrative receiverships, but also incur higher costs. The net result is that creditors' recoveries are no better under the new system;
- » administrations do not result in more "going concern" sales than administrative receiverships, and therefore they are not more effective at preserving employment. Indeed, the insolvency practitioners interviewed stated that administrations for the purpose of corporate rescue were rare (if such an outcome is possible, it is more common for the company to be restructured outside of formal insolvency proceedings); and
- » the administrations are concluded, on average, in almost half the time of administrative receiverships (compare an average of 356 days to 622 days).

Therefore, although new administrations have achieved their goal of enfranchising all of the creditors and making insolvency practitioners more accountable, they have not seen a rise in creditors' recoveries or corporate rescues. The interview evidence suggested that administrations are being used as a substitute for liquidation as well as administrative receivership. Another explanation lies in changes in banking practice. Interviewees expressed the opinion that banks were less willing to provide overdraft finance for working capital, so companies were having to look to other source, such as asset-based finance, instead. With more fragmented financing, conflicts between creditors were more likely and there was less concern from the creditors about their relationship with the company.

"The Impact of the Enterprise Act 2002 on Realisations and Costs in Corporate Rescue Proceedings" by John Armour, Audrey Hsu and Adrian Walters can be freely downloaded from the Insolvency Service's website: <http://www.insolvency.gov.uk/>

▶ Contents

▶ News

▶ Cases

▶ Legislation

▶ Focus on...

▶ CA 2006

▶ All newsletters

▶ Online updates

▶ Email us



PDF printer
friendly version

News



RECENT CASES

Director's breach of fiduciary duties

See CLM: ¶2392, ¶2406

Foster Bryant Surveying Ltd v Bryant, and Savernake Property Consultants Ltd [2007] EWCA Civ 200

A director has been held not to have breached his fiduciary duties **during his notice period**, despite arranging to **work for his company's principal client**. The Court of Appeal stressed that this case, as with all breach of fiduciary duties cases, was decided on its particular facts and that a similar case had not been before the courts before.

Mr B and Mr F were the only two directors of FBS Ltd, a company which undertook surveying and project management work mostly from one client, ALS Ltd. Mr B, Mr F and Mrs B were all chartered surveyors at FBS Ltd. Mr B and Mr F also held the company's shares, 40% and 60% respectively. Mr B obtained two other clients, but FBS Ltd lost that work when one of them was taken over by another company and the other went into receivership. This triggered the breakdown in the relationship between the two directors, with Mr F blaming Mr B for the loss of these clients. When Mr F announced that Mrs B was being made redundant, Mr B also handed in his resignation. He left the company 2 months later.

Mr B informed ALS Ltd that he had resigned the following day, as a matter of professional courtesy. ALS Ltd then approached Mr B to ask if he would continue to work with ALS Ltd when he joined another firm or whether he would like to work for ALS Ltd directly. ALS Ltd was concerned about providing a consistent level of service for its clients, who had been happy working with both Mr B and Mr F. He said he would think about it, and over the following couple of weeks they discussed the options and he agreed to work for ALS Ltd on a retainer basis. Meanwhile, ALS Ltd offered to continue to provide FBS Ltd with as much work as Mr F could perform, but this proposal was rejected. During his notice period, Mr B continued to work for FBS Ltd; he was still a director according to the shareholders' agreement, but he was not involved in company management or decision making in this capacity and Mr F had filed Form 288b in respect of Mr B at Companies House.

FBS Ltd claimed that Mr B was in breach of his fiduciary duties to it and that he should be liable to account for the profit he made from carrying on work which would otherwise have been done by FBS Ltd.

In the particular **circumstances of this case**, the court found that Mr B was not in breach of his fiduciary duties to FBS Ltd. He had not sought work from ALS Ltd, and he did not start working for ALS Ltd until after his resignation took effect. He had no ulterior motive for resigning; there was no evidence of disloyalty or conflict of interest. Further, on the evidence presented, the court was not able to make a finding that any specific business opportunities or property had been taken or exploited by Mr B.

Payment of fee to introducing agent not financial assistance

See CLM: ¶5569+

Corporate Development Partners LLC v E-Relationship Marketing Ltd [2007] EWHC 436 (Ch)

The court has held that a fee payable by a company to an agent who introduced the company to the buyer of its shares did not constitute financial assistance. The question to be answered was whether, as a matter of commercial reality, the company's commitment to pay the agent a fee if the buyer completed the purchase amounted to the provision of any relevant "financial assistance" to anyone which was directly or indirectly "**for the purpose**" of that acquisition. The answer in any particular case is likely to be fact-sensitive.

In this case, after the introduction, the agent played no role in the negotiation of the acquisition and was neither intended nor required to. The payment of the fee was not a condition of the acquisition; it would not serve to reduce the buyer's acquisition obligations by a single penny; and it was neither intended to, nor did it, smooth the path towards the acquisition. Therefore, although the reason for the payment was because the agent had introduced a party which had acquired the company, it was not "for the purpose" of the acquisition.

- ▶ Contents
- ▶ News
- ▶ Cases
- ▶ Legislation
- ▶ Focus on...
- ▶ CA 2006

- ▷ All newsletters
- ▷ Online updates
- ▷ Email us



PDF printer friendly version



RECENT CASES cont...

It is generally prohibited for a company to give financial assistance for the purpose of an acquisition of its own shares (see ¶15557+). The prohibition is drawn widely and has been held to include payment of the fees of the seller's or buyer's professional advisers.

Meaning of “reasonable endeavours”

See CLM: ¶15762+

Rhodia International Holdings Ltd v Huntsman International LLC [2007] EWHC 292 (Comm)

In a recent decision concerning whether a buyer of a business had used its reasonable endeavours to obtain the novation of one of the business' contracts, the court considered the meaning of that phrase.

As regards the relationship between the phrases “reasonable endeavours” and “best endeavours”, it found that:

- » an obligation to use reasonable endeavours probably only requires a party to take one reasonable course of action, not all of them;
- » an obligation to use best endeavours probably requires a party to take all the reasonable courses of action he can;
- » therefore, it may well be that an obligation to use all reasonable endeavours equates with using best endeavours; and
- » an obligation to use reasonable endeavours is less stringent than one to use best endeavours.

As regards **what reasonable endeavours actually entail**, the court found that they do not require a party to sacrifice its own commercial interest, subject to one important exception: where the contract specifies that certain steps have to be taken as part of the exercise of reasonable endeavours. If the contract does specify other steps, they will have to be taken, even if that could involve the sacrificing of a party's commercial interests.

In the case before the court, the buyer was obligated to enter into a direct covenant with the other party to the contract which was being novated, if requested to do so. The buyer had carried out the business acquisition through a newly incorporated special purpose vehicle so the other party requested a parent company guarantee from the buyer as a condition of novation. The buyer refused to give the guarantee, the contract was not novated and eventually the other party sued the seller (as the original contracting party) for non-performance. Since the buyer had not given the parent company guarantee when requested, the court found that it had failed to use its reasonable endeavours to obtain the novation and was liable for the non-performance.

Can rates be paid as an expense of administration?

See CLM: ¶18927

Exeter City Council v Bairstow, Martin and Trident Fashions plc [2007] EWHC 400 (Ch)

In the first case to be brought on this question in relation to **post-Enterprise Act administrations**, a local council applied for a declaration that **non-domestic rates** in respect of premises occupied by a company in administration should be payable out of the company's assets as an expense of the insolvency procedure.

Existing case law established that rates were not payable as expenses of administration in respect of “old” administrations (*Centre Reinsurance International Co v Freakley* [2006] 4 All ER 1153). However, there was no provision in the Rules setting out which expenses could be paid out of the company's assets in respect of these administrations. The Rules now set out an order of priority for certain expenses which can be paid out of the company's assets in the case of “new” administrations, similar to the provisions in liquidation (see CLM ¶17958). In respect of liquidation, case law has established that rates accruing on premises occupied by a company are payable as an expense of the liquidation, under the category of “disbursements” (*Re Toshoku Finance UK plc* [2002] 3 All ER 961).

Since this was a case on such an important point which would affect the conduct of most administrations, the court sought the views of the insolvency practitioners' profession as well as

▶ Contents

▶ News

▶ Cases

▶ Legislation

▶ Focus on...

▶ CA 2006

▷ All newsletters

▷ Online updates

▷ Email us



PDF printer
friendly version

Case law



RECENT CASES cont...

considering how the issue is dealt with in other types of insolvency proceedings. The profession advanced several **arguments** against categorising rates as expenses of the administration, including that the cost may prevent administrators from conducting as many administrations as going concerns, secured lenders may be more reluctant to fund company rescues as they would be deferred to another priority claim, and the company's unsecured assets and floating charge realisations would be depleted further, making it difficult to meet other expenses and claims.

The **court concluded** that non-domestic rates were payable as expenses of administration, under the category of disbursements. The relevant Rule for new administrations had been modelled on that for liquidation, and case law had interpreted the liquidation Rule as including rates. The question of what should be paid out of a company's assets while it is subject to an insolvency procedure is a matter of policy, to be determined by the rule-making authorities, not the courts. Since the Insolvency Service must have been aware of the *Re Toshoku Finance UK plc* decision when it formulated the Rule for new administrations, the court felt that it had to respect that policy decision.

The relevant **Rules** are: r 2.67(1)(f) IR 1986 for administration, and r 4.218(1)(m) IR 1986 for liquidation. It will be interesting to see whether the Insolvency Service takes the opportunity during its review of secondary legislation to disagree with this decision when it drafts the new Insolvency Rules.

- ▶ [Contents](#)
- ▶ [News](#)
- ▶ [Cases](#)
- ▶ [Legislation](#)
- ▶ [Focus on...](#)
- ▶ [CA 2006](#)

- ▷ [All newsletters](#)
- ▷ [Online updates](#)
- ▷ [Email us](#)



PDF printer
friendly version

Case law



LEGISLATION

Winding up petition deposit increase

See CLM: ¶7639, ¶7640, ¶7659

As of 1 April 2007 the deposit to be submitted when filing a winding up petition at court will increase from £655 to £670 (SI 2004/593 as amended by SI 2007/521).

DTI consultations on implementation of EC Directives

The DTI has published consultation papers on the implementation of four EC Directives.

EC Directive on capital maintenance and share capital

See CLM: ¶730

As part of its consultation on implementation of the Companies Act 2006, the Government has published its consultation on implementation of the EC Directive on capital maintenance and share capital (EC Directive 2006/68).

The Government's view is that although the limited amendments permitted by the Directive might provide some additional degree of flexibility for companies, it will increase legislation in an already complex area of company law. Further, UK law is considered to be wholly consistent with its provisions. As a result, **the Government does not propose to take any further action** to implement the Directive.

The consultation can be found at paragraphs 6.8 to 6.23 of "Companies Act 2006 – A Consultative Document", which may be downloaded from the DTI's website (www.dti.gov.uk/bbf/co-act-2006/index.html). Comments are requested by 31 May 2007.

EC Directive on company reporting

See CLM: ¶4226+

On 5 March 2007, the DTI began consulting on proposals to implement the new EC Directive on company reporting (EC Directive 2006/46) which must be **implemented into national law** by 5 September 2008. The Government intends to include the necessary provisions in the package of secondary legislation that will implement the accounting provisions in the Companies Act 2006.

The main proposals are:

- » to increase the thresholds for **small company/group status** to £6.5 million (turnover) and £3.26 million (balance sheet total);
- » to increase the thresholds for **medium-sized company/group status** to £25.9 million (turnover) and £12.9 million (balance sheet total);
- » to permit, but not require, all companies preparing accounts under the Companies Act using UK Financial Reporting Standards (FRS) to use **fair value** in accordance with IAS 39 in both their individual and consolidated accounts. The ASB will consider what, if any, action needs to be taken in respect of UK accounting standards;
- » to require all medium-sized and large companies to disclose **off-balance sheet arrangements** (medium-sized companies will be allowed to limit their disclosure to information about the nature and business purpose of the arrangements);
- » to require all medium-sized and large companies which prepare Companies Act accounts using UK FRS to disclose **related party transactions** (there will be an exception for transactions in a group provided any subsidiaries involved are wholly-owned; the Government is considering whether any exemptions should apply to medium-sized companies); and
- » to require listed companies to produce an **annual corporate governance statement** in the annual (directors') report or as a separate report.

The consultation paper can be downloaded from the DTI's website (www.dti.gov.uk/consultations). Comments are requested by 1 June 2007.

▶ Contents

▶ News

▶ Cases

▶ Legislation

▶ Focus on...

▶ CA 2006

▶ All newsletters

▶ Online updates

▶ Email us



PDF printer friendly version

Legislation



LEGISLATION cont...

EC Directive on statutory audits

See CLM: ¶4290+

On 5 March 2007, the DTI began consulting on proposals to implement the new EC Directive on statutory audits (EC Directive 2006/43) which must be **implemented into national law** by 29 June 2008. The Government plans to bring into force the majority of implementing regulations in April 2008. The provisions would apply to reporting periods beginning on or after the date when the regulations come into force.

The main proposals are:

- » to make new regulations regarding the maintenance of a **public register of auditors**. This will be fully operational by June 2009;
- » to amend the new Companies Act (Sch 10 CA 2006) so that an outgoing auditor will be obliged to provide all relevant **information to the incoming auditor**. The detail of this provision will be set out in rules of the recognised supervisory bodies who are responsible for supervising the auditors registered with them (currently these are ICAEW, ICAS, ICAI, ACCA and AAPA);
- » to amend the Ethical Standards set by the Auditing Practices Board so that **audit fees** cannot be influenced or determined by the provision of additional services to the audited company nor based on any form of contingency;
- » to ensure that statutory auditors (whether individual or firms) may be **dismissed only where there are proper grounds**. Currently, the Government prefers that: the dismissal of an auditor without proper grounds should be treated as unfairly prejudicial to the shareholders entitling them to make an application to court; and the court should be able to order the re-appointment of the original auditors, the appointment of new auditors, or any other remedy which it deemed appropriate;
- » to amend the regulations regarding the **disclosure of auditor remuneration** so that medium-sized companies will have to supply additional information on non-audit services in response to a request from the Professional Oversight Board. The Government is considering whether the same should apply to small companies who have an audit;
- » various provisions relating to the **audit of public interest entities** (these are listed companies, banks and building societies and insurance undertakings); and
- » various provisions relating to **third country auditors** (these are the auditors of non-EU companies who are listed on an EU regulated market).

The consultation paper can be downloaded from the DTI's website (www.dti.gov.uk/consultations). Comments are requested by 1 June 2007.

EC Directive on cross-border mergers

See CLM: ¶6530+

On 5 March 2007, the DTI began consulting on proposals to implement the new EC Directive on cross-border mergers (EC Directive 2005/56) which must be **implemented into national law** by 15 December 2007. The Directive introduces for the first time a legislative framework that enables cross-border mergers between companies in the EEA; UK law does not provide for cross-border mergers at present. The Government plans to implement the Directive by a single set of self-standing regulations which will come into force on 15 December 2007.

The new law will apply only where there is a **genuine cross-border element** to the merger. This means that the merger must involve at least two companies governed by the laws of different member states. It is proposed that the **types of companies** which may be involved in the merger are:

- » public and private companies limited by shares or guarantee;
- » unregistered companies; and
- » unlimited companies.

The proposed merger procedure is similar to the current UK law on domestic mergers of public companies (see ¶6536+). It will allow for three **types of merger**:

- » merger by absorption (where an existing company absorbs one or more other merging companies);
- » merger by formation of a new company (where two or more companies merge to form a new company); and
- » merger by absorption of a wholly owned subsidiary.

▶ Contents

▶ News

▶ Cases

▶ Legislation

▶ Focus on...

▶ CA 2006

▶ All newsletters

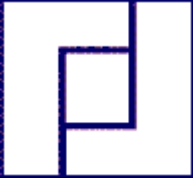
▶ Online updates

▶ Email us



PDF printer
friendly version

Legislation



LEGISLATION cont...

The Directive also requires **employee participation** in the merger where such arrangements exist in one or more of the merging companies. Employee participation means the right of employees to influence board appointments. This right does not exist in the UK, although there is nothing to prevent employers and employees from creating such arrangements voluntarily. Employee participation does exist in other member states (such as Germany, Austria, the Netherlands and Sweden). Therefore, a company resulting from a cross-border merger that has its registered office in the UK may have to provide for employee participation. The proposed employee participation arrangements are similar to the current UK law on establishing a European Company (see ¶95+).

The consultation paper can be downloaded from the DTI's website (www.dti.gov.uk/consultations). Comments are requested by 1 June 2007.

Comment: In the UK, corporate restructuring practice has seen greater use of **takeovers** rather than mergers. As part of the consultation, the Government is asking for views on whether companies would consider using the merger framework to undertake a cross-border merger in the EEA. It will be interesting to see whether the market feels the need for this procedure.

▶ Contents

▶ News

▶ Cases

▶ Legislation

▶ Focus on...

▶ CA 2006

▷ All newsletters

▷ Online updates

▷ Email us



PDF printer
friendly version

Legislation



THE CORPORATE MANSLAUGHTER BILL

A new draft of the Corporate Manslaughter and Corporate Homicide Bill was published last month. This area remains so contentious that the Bill's passage through Parliament is under threat even at this late stage. This article explores the need for a corporate killing offence and why the Government's proposed solutions have caused such a fierce debate.

- ▶ Contents
- ▶ News
- ▶ Cases
- ▶ Legislation
- ▶ Focus on...

▶ CA 2006

▶ All newsletters

▶ Online updates

▶ Email us



PDF printer
friendly version

There is little argument about the necessity for the Corporate Manslaughter and Corporate Homicide Bill. The current common law position has failed to exact justice in so many high-profile cases that there is a real public interest need for the issue to be tackled in legislation.

As the law **currently** stands, a company can be prosecuted for the offence of "gross negligence manslaughter" of a person where (*R v Adomako* [1994] 3 All ER 79):

- » it owed a duty of care to that person; and
- » breach of that duty was the substantial cause of his death, or the breach was so grossly negligent as to show such a disregard for his life that it warrants criminal punishment.

However, in order for a company to be convicted of a common law crime, it must be shown that a person or persons acting as the "directing mind of the company" had the requisite intent to commit the crime because the company, being an artificial "legal" person rather than an individual, cannot be said to "intend" to do anything (*R v ICR Haulage Ltd* [1994] 1 All ER 691). To apply this "identification principle" to the offence of gross negligence manslaughter, the prosecution must therefore establish that an individual or individuals embodying the company is/are guilty of manslaughter.

Although successful prosecutions have been brought against individuals for manslaughter, against individuals and companies for breaches of health and safety law and companies have been sued in the civil courts for negligence, prosecutions against companies for gross negligence manslaughter fail or are not pursued because of the difficulty in applying the identification principle. For example, the court is due this week to set the level of Network Rail's fine for the health and safety breaches of its predecessor, Railtrack, which contributed to the Paddington rail crash. Although the health and safety cases against Thames Trains and Railtrack revealed serious failings in management and practice (so much so that the £2million fine imposed on Thames Trains in 2004 set a record at the time), the CPS decided that there was not enough evidence to charge either company with gross negligence manslaughter. The main problem with such cases is that even where an individual at fault can be identified, it is extremely difficult to show that he was the "directing mind" of the company, especially in large companies with complex management structures. Therefore, in the cases where there is arguably the greatest public interest in seeing justice done, such as public transport disasters, companies are seen literally to get away with murder.

The discussion of the Bill here is based on the version as amended by the House of Lords on report (HL Bill 40 06-07), which can be found on Parliament's website:

<http://www.publications.parliament.uk/pa/pabills.htm#c>

The offence

The Corporate Manslaughter and Corporate Homicide Bill proposes to introduce an offence of corporate manslaughter (called "corporate homicide" in Scotland) of which a company will be guilty if the way in which its activities are managed or organised (s 1):

- » causes a person's death; and
- » amounts to a gross breach of a relevant duty of care owed by the company to the deceased.

The offence will **apply to** companies, those public bodies and government departments listed in Schedule 1 to the Bill, police forces and other employers (including partnerships, trade unions and employers' associations). However, the focus here is on companies.

The Bill provides further explanation of the various components of the offence.

A company will only be able to be found guilty of the offence if the management or organisation of its activities by its **senior management** was a substantial element in the breach (s 2). The senior management comprises persons who play significant roles in making decisions about, or managing or organising, the whole or a substantial part of

Focus on...



THE CORPORATE MANSLAUGHTER BILL cont...

▶ Contents

▶ News

▶ Cases

▶ Legislation

▶ Focus on...

▶ CA 2006

▶ All newsletters

▶ Online updates

▶ Email us



PDF printer
friendly version

- the company's activities. This has become known as the "senior management failure" test.
- » A **relevant duty of care** means duties of care owed in negligence (s 3):
 - to employees and others providing services;
 - as an occupier of premises;
 - as the supplier of goods or services;
 - in carrying out construction or maintenance services;
 - in carrying out any other commercial activity;
 - in using or keeping any plant, vehicle or other item; and
 - to a person held in custody.
 - » A **breach will be "gross"** if the conduct said to amount to the breach falls far below what could reasonably be expected of the company in the circumstances (s 2). This will be a question for the jury to decide, taking into account as part of its deliberation failures to adhere to health and safety legislation and guidance, as well as the attitudes, policies, systems or accepted practices within the company which were likely to have encouraged a failure to adhere to health and safety legislation (s 8).

The main criticism levied against this formulation of the offence is that it is not all that different from the common law offence of gross negligence manslaughter. It still relies heavily on the actions or omissions of a person or persons at a high level in the company's management, giving rise to concern that the **senior management failure test** will be as difficult to apply as the identification principle. Some very high thresholds will have to be met:

- » the senior management's organisation/management of the company's activities must be a *substantial* element in the *gross* breach of duty owed to the deceased; and
- » only persons with *significant* roles in managing, organising or making decisions relating to the *whole* or a *significant part of the company's activities* form part of its senior management.

The upshot of this is that it will still be very difficult, particularly where a case is brought against a large company, to satisfy the senior management failure test. In large companies, it is more likely that the board and senior management figures are removed from decisions affecting health and safety issues, and the junior managers or external contractors who do have this responsibility will not qualify as "senior management". Even many senior figures in a company, such as directors with responsibility for a discrete area of the business, will not meet the requirement of playing a significant role in a significant part of the company's activities. Of course, the test should not be so easy to satisfy that companies are unjustly convicted, but there is concern that the new test does not overcome the difficulties of the current one.

There is also concern that the **drafting** of the offence and definitions will expose it to semantic argument in court, which could result in cases failing for "technical" reasons. For example, will the requirement for the offence to be committed in the "way in which [a company's] activities are managed or organised" be wide enough to include the situation where a company's shortcomings are not down to how the senior management actively conducts its affairs, but rather are a result of historical, deep-seated bad management? Not specific failures as such, but a culture of inadequacy.

The punishment

The offence will be punishable on indictment, rendering defendant companies liable to a **fine** (s 1). There is, of course, no other punishment that can be levied against a company. There is concern that this will not have the "deterrent" effect that imprisoning senior management figures would have. However, a charge of corporate manslaughter would have to be brought against the company, not the individuals involved, and other "corporate" offences which can result in an officer's imprisonment apply to both companies and officers. Individuals will still be able to be prosecuted separately for the death where appropriate, but the Bill specifically precludes their prosecution for aiding, abetting, counselling or procuring corporate manslaughter (s 18). The purpose of the Bill is to hold companies accountable for deaths they have caused, so it is right that a company should be punished as a separate entity.

The court will also be able to impose "**remedial orders**" on companies convicted of corporate manslaughter, to ensure that they remedy the breach, any other cause of the death and/or any other health and safety deficiency (s 9). Coupled with this practical remedy, the court will also be able to order that a company's conviction and punishment is **publicised** (s 10). The effect of a successful prosecution on the reputation of the company and its management (even if they are not prosecuted individually) will provide a strong "deterrent factor".

Focus on...



THE CORPORATE MANSLAUGHTER BILL cont...

Exceptions to the offence

The Bill includes various exceptions. Broadly, these are:

- » duties of care owed by public authorities (s 3):
 - regarding public policy decisions; and
 - in respect of the exercise of a public function or statutory inspections other than towards their employees and service providers, as occupier and towards anyone held in custody;
- » duties of care owed by the MoD in respect of operations (s 4);
- » duties of care owed by public authorities in respect of policing and law enforcement operations (s 5);
- » duties of care owed by the fire services, NHS and ambulance services, rescue services and the armed forces in respect of the way in which they respond to emergencies other than giving or deciding on medical treatment (s 6); and
- » statutory duties of care owed by local and public authorities and local probation boards in respect of child-protection and probation functions (s 7).

These exceptions are significant because they exclude the main circumstances in which public bodies and organisations are likely to cause death. The Government's justification for this is that these bodies are adequately supervised, any deaths caused by them are investigated separately and that it would not be appropriate for public policy and resources to be discussed in a court of law. The House of Lords has amended the Bill to prevent **deaths in custody** from falling within the exceptions. The effect of the original exclusion of duties owed to persons in custody would have rendered the police force or prison service liable to a prosecution for corporate manslaughter if a person in custody died as a result of a breach of its duty as occupier (e.g. because the ceiling of the cell collapsed), but not for using an illegal method of restraint. On 5 February, the House of Lords voted overwhelmingly in favour of altering this particular exception to include any death in custody in the Bill.

What next?

The Bill received its third reading in the House of Lords at the end of February and the Lords have published their amendments. Its future is uncertain: the Government has threatened to drop the Bill altogether rather than accept the Lords' proposed amendment on deaths in custody, so it will be interesting to see how the Commons responds to the return of the Bill at this final "ping pong" stage (where the Bill will pass between the two houses as amendments are debated). What is certain is that the current common law position has failed to address the public interest need to convict companies of corporate manslaughter in appropriate cases and that a replacement offence is needed. However, the Corporate Manslaughter and Corporate Homicide Bill's progress through parliament has shown how difficult it is to formulate an effective offence which protects people but does not stifle business.

▶ Contents

▶ News

▶ Cases

▶ Legislation

▶ Focus on...

▶ CA 2006

▷ All newsletters

▷ Online updates

▷ Email us



PDF printer
friendly version

Focus on...



COMPANIES ACT 2006: IMPLEMENTATION

The Companies Act 2006 received Royal Assent on 8 November 2006.

The final **text** of the Act, explanatory **notes and tables** of destinations and origins are now freely available to download at: <http://www.opsi.gov.uk/acts/acts2006a.htm>

The Government has announced its **timetable** for implementing the Companies Act 2006. To see when specific sections of the Act will or have come into force, check the *implementation timetable* on the FL Memo Ltd newsletter homepage (follow the link to "Companies Act 2006 implementation timetable"). This document will be updated as new secondary legislation is passed.

For more information on provisions of the Act which are **already in force**, and which are due to come **into force on 6 April 2007**, see *Company Law Memo 2006 Issue 9*. Changes to the City Code as a result of the coming into force of Part 28 of the Companies Act 2006 on Takeovers are discussed earlier in this Newsletter, in *News*.

Also see *Company Law Memo 2006 Issue 9* for a summary of ICSA's guidance on the new company communication provisions.

- ▶ Contents
- ▶ News
- ▶ Cases
- ▶ Legislation
- ▶ Focus on...
- ▶ CA 2006

- ▷ All newsletters
- ▷ Online updates
- ▷ Email us



PDF printer friendly version

DTI Consultation

On 28 February, the Government published its first major consultation on implementation of the new Act. "Companies Act 2006 – A Consultative Document" (February 2007) is available to download from the DTI's website at <http://www.dti.gov.uk/bbf/co-act-2006/index.html>. Comments are requested by 31 May 2007 (except for comments on political donations and expenditure, which are requested by 1 May 2007).

The current consultation sets out the Government's proposals on some **secondary legislation** and **transitional arrangements**. These are considered below, topic by topic.

Overseas companies

See *CLM*: ¶140, ¶168, ¶177

At present, there are two registration regimes governing overseas companies which operate in the UK: the "branch" regime and the "place of business" regime. In recognition of the confusion this causes, the new Companies Act allows the Government to standardise the **registration regime** by regulations. The Government has announced that it intends to base the new regime on the existing concept of "branch" only. This means that companies which operate a place of business in the UK, but not a branch, would no longer be required to register with Companies House. The new regime would apply to branches of companies from other EU member states; the Government is considering whether the same or different registration arrangements should apply to non-EU companies who carry on business in the UK.

The Government has also proposed some changes to when an overseas company would have to register a **mortgage or charge over its UK property**. The proposal is that registration of specified mortgage and charges would only be required if the overseas company were registered with Companies House; it would not apply if the company were not required to register or failed to do so. This would do away with the "Slavenburg" index (an unofficial register of mortgages and charges over unregistered overseas companies maintained by Companies House).

The **sanctions for non-registration** would be slightly different too. If the mortgage or charge related to the UK property of a registered overseas company, it would be invalid if not registered within 21 days of creation (i.e. the same sanction that would apply to the non-registration of a mortgage or charge by a UK company). However, only a fine would apply if the company had not yet registered as an overseas company and failed to register the charge when it registered its presence or if the failure related to property which had been brought into the UK after the mortgage or charge was created.

Finally, the Government has made some proposals regarding the disclosures which an overseas company will have to make on its stationery and signs. The proposal is that non-EU overseas companies will be required to **disclose its name and registration details** in its business letters and order forms, whether the document is in hard copy or electronic or any other form, and also in any .uk websites.

CA 2006



COMPANIES ACT 2006: IMPLEMENTATION cont...

Company names

See CLM: ¶248, ¶254

The new Companies Act allows the Government to pass regulations on what letters, symbols etc. may be used in a company name and any prohibited words or expressions. The Government has published a set of uncontroversial proposals which:

- » list a comprehensive set of acceptable characters and symbols;
- » largely replicate the current list of prohibited words or expressions; and
- » limit the length of a company name to 160 characters.

Trading disclosures

See CLM: ¶259, ¶585, ¶7750, ¶8229, ¶8468

Companies are required to publicise certain information about themselves so that members of the general public can easily identify which company they are dealing with. The new Companies Act does not include the detail of required disclosures. Instead, this will be set out in regulations. The rules have already been expanded recently to require companies to make these disclosures on websites and order forms as well as letters and invoices (see *Company Law Memo 2006 Newsletter Issue 8*), and the Government plans to expand the requirements further by requiring a company's name to appear **on all documents and communications**, whatever form they are in. Having one rule that applies to all documents should make it easier for companies to comply.

Articles of association

See CLM: ¶435+

Following their consultation on the draft **model articles** for private companies limited by shares and public companies, the Government has issued **new drafts** for these types of company. It has also published for the first time draft model articles for private companies limited by guarantee, which closely follow those for private companies limited by shares. The Government has confirmed that model articles will only be specified for these three types of company; other types, such as unlimited companies, will be expected to produce bespoke articles.

The type of model articles that will **apply** to a company will depend upon its type at formation. Therefore, if a private company limited by shares re-registers as a public company, it will have to make any relevant alterations to its articles to reflect its new status. As with Table A, the new model articles for both types of private limited company are intended to be "default" articles, which could work in their own right but will often be tailored by individual companies. The Government acknowledges that public companies are far more likely to have specifically drafted articles, and therefore sees their new model articles being used as more of a drafting tool rather than a complete template. The model does not seek to satisfy the requirements or best practice for listed companies. The Government intends to publish non-statutory **guidance** on using the different sets of model articles in due course.

Several changes have been made to the new draft model articles for private companies limited by shares and public companies. The main change from previous drafts is that the model articles for private companies now include provisions relating to shareholder decision making. Unfortunately, this means that many of the references to specific regulations of the previous drafts given in *Company Law Memo 2007* have been superseded. A **destination table** for the draft new model articles for private companies limited by shares and public companies is available on the FL Memo newsletter homepage, so subscribers who are interested in the specific provisions can update their references and follow future changes (follow the link to "Draft Model Articles Destination Table").

As far as the **timetable** for bringing these articles into force is concerned, the Government intends to pass the necessary regulations in autumn 2007 to come into effect from October 2008. This is when the provisions enabling companies to be formed under the new Act will be brought into force. Any companies which have been formed before October 2008 will continue to be governed by their own specific articles or the applicable Table A, unless they change their articles.

Company formations

See CLM: ¶517+

The new Act sets out a completely new procedure for company formations. However, some of the content of the various documents that would have to be filed at Companies House was left

▶ Contents

▶ News

▶ Cases

▶ Legislation

▶ Focus on...

▶ CA 2006

▷ All newsletters

▷ Online updates

▷ Email us



PDF printer
friendly version

CA 2006



COMPANIES ACT 2006: IMPLEMENTATION cont...

to regulations. The Government has now announced that it proposes that each of the **memorandum, statement of capital and initial shareholdings** and **statement of guarantee** will have to contain the individual names of the subscribers. The subscribers will each have to authenticate the memorandum, but there will be no need for a witness (Companies House will be consulting on authentication rules in due course). An address will have to be provided for each subscriber. This could be a service address, but not a PO Box. Any subscriber who is a UK company will have to provide its registered office address.

Public company share capital

See CLM: ¶703, ¶715, ¶1325

The Companies Act 2006 requires a public company to have a share capital of at least £50,000, or the equivalent in euros (but not a combination of the two). The Government has announced that it will not be exercising its power in the Act to change this amount. It will be passing regulations to prescribe the amount in euros that is to be treated as equivalent to £50,000. This will only be revisited when currency fluctuations result in it differing significantly from £50,000.

The new Act also introduces a new procedure for the redenomination of shares. If a public company redenominates its shares out of sterling, currency fluctuations could result in its share capital falling below £50,000. Normally, this would require it to re-register as a private company. The Government proposes that currency fluctuations resulting in a change in the sterling value of a public company's share capital should be ignored except for when the court sanctions a reduction of capital or the company redenominates its shares. In those two circumstances, a theoretical conversion of the company's share capital would take place to see whether the company still satisfies the authorised minimum. If not, the company would be subject to an expedited procedure for re-registering as a private company.

Share issues and allotments

See CLM: ¶1087

Under the Companies Act 2006, new forms will have to be filed at Companies House following an allotment of shares: the **statement of capital** and a new return of allotment. The statement of capital will have to contain information about the particular rights of the shares that have been allotted. The Government has announced that these will be the right to vote, participate in dividends and receive a return of capital in a winding up. If the statement is made in connection with an allotment of redeemable shares and the directors are authorised to set the terms and manner of redemption, it will also have to set out those terms.

The Government has also announced the information which will have to be set out in the **return of allotment**. Companies will no longer have to provide the names and addresses of the allottees nor, if the allotment is for non-cash consideration, will they have to supply a copy of the contract or particulars of the contract if it is not in writing. Instead, they will have to provide details of any non-cash consideration on the return.

Reduction of capital

See CLM: ¶1469

The new Act contains a new reduction of capital procedure which does not require the approval of the court. The Government has announced that it proposes to restrict the availability of reserves created by a reduction under the new procedure. This is to protect creditors, whose consent would not be required for the reduction and for whom the company would not have to provide security, unlike in the current court-approved procedure. The restriction is that such reserves will not be distributable. Instead, they will be treated as realised profit which, in accordance with GAAP, may be offset against the company's realised losses for the purposes of calculating whether the company may pay a dividend.

Directors

See CLM: ¶2242

The new Companies Act will require every company to have **at least one director who is an individual**. The Government is considering allowing a grace period after the commencement of this requirement (in October 2008) to allow companies which do not comply to make a suitable appointment.

▶ Contents

▶ News

▶ Cases

▶ Legislation

▶ Focus on...

▶ CA 2006

▷ All newsletters

▷ Online updates

▷ Email us



PDF printer
friendly version

CA 2006



COMPANIES ACT 2006: IMPLEMENTATION cont...

Residential addresses

See CLM: ¶2250, ¶3896, ¶3899, ¶3918+, ¶4064

The new Companies Act will not require **directors'** residential addresses to appear on the public record at Companies House or in the company's statutory books. Instead, an address for service will have to be provided for general communication. Although directors' home addresses will have to be filed at Companies House, they will be "protected". This means that they will only be made available to public authorities (including enforcement bodies) and credit reference agencies.

The Government has issued a list of designated public authorities that will have access to this information, and proposes to restrict their use of it to circumstances falling within their "public function". It is proposed that credit reference agencies will only be able to use the information to process applications for credit and to carry out their money laundering checks.

A further level of protection will be available where a company is likely to be subject to violence or intimidation or the director (or prospective director) is engaged by the security and intelligence services or the police. Such a (prospective) director will be able to apply to Companies House for his residential address not to be disclosed to credit reference agencies either. Significantly for directors currently in office, if a confidentiality order is already in place, this protection will automatically apply.

As for directors' residential addresses which are already on the register, Companies House has indicated that it will be able to remove them (on application) if they were filed on or after 1 January 2003. Before that date, the records are held on microfiche and are too difficult to remove without damaging the rest of the record.

There is no requirement for **shareholders'** residential addresses to be on the public record. However, an address is required and many shareholders enter their home addresses as they do not have a separate service address. The new Companies Act will still require every shareholder's name and address to appear on the register of shareholders. The information required on the annual return, however, is to be set out in regulations. The Government proposes that only public companies with shares traded on an EU regulated market will have to disclose its shareholders' addresses, and even then it will only apply to shareholders with 5% or more of the company's shares. In any event, these shareholders are likely to have service addresses they can use instead of their residential addresses, minimising the risk of misuse of their personal information.

Where a shareholder's address is already on the public register, he will be able to apply for it to be removed on the grounds that the company is likely to be subject to violence or intimidation, or that the individual works for the security and intelligence services. Only addresses filed on or after 1 January 2003 will be able to be removed.

Applications to remove other addresses, for example, those for companies' registered offices or secured lenders, will be able to be made on the same grounds (provided they were filed on or after 1 January 2003).

Political donations

See CLM: ¶3204

To accompany the implementation of the provisions of the new Act relating to political donations, the Government proposes to make regulations which will **except certain types of company** from the restrictions, e.g. media companies, which prepare, publish and disseminate material about political and current affairs. Separate regulations will set the **rate of interest** payable on unauthorised donations or payments at 5% per annum. Consultation on these regulations is due to close on the earlier date of 1 May 2007 because these provisions are scheduled to come into force in October 2007.

The Government proposes that **existing resolutions** allowing donations to be made when the relevant provisions come into force will still be valid. Since donations to **independent election candidates** will also be caught under the new provisions, the Government is considering introducing transitional arrangements to defer commencement as regards these candidates to enable companies to pass new or wider resolutions. Consultation on both of these transitional arrangements is due to close on 1 May 2007 as well.

▶ Contents

▶ News

▶ Cases

▶ Legislation

▶ Focus on...

▶ CA 2006

▷ All newsletters

▷ Online updates

▷ Email us



PDF printer
friendly version

CA 2006



COMPANIES ACT 2006: IMPLEMENTATION cont...

▶ Contents

▶ News

▶ Cases

▶ Legislation

▶ Focus on...

▶ CA 2006

▷ All newsletters

▷ Online updates

▷ Email us



PDF printer
friendly version

Extraordinary resolutions

See CLM: ¶3544, ¶8087, ¶8216, ¶8438, ¶8515, ¶8615

The new Companies Act does not specify how references to extraordinary resolutions in companies' articles and other documents should be interpreted after the new provisions relating to resolutions and meetings come into force in October 2007. The Government is inviting views on whether this question should be left to the courts or dealt with in transitional arrangements.

Company records

See CLM: ¶3889, ¶3928, ¶3930, ¶3936, ¶3976, ¶3977, ¶3993, ¶3994, ¶4006, ¶4007, ¶4019

The Government has proposed that the shorter retention period in the new Act for information in the register of shareholders should apply immediately from commencement of the relevant provision in October 2008. This would enable companies to dispose of any records over 10 years old straight away, instead of having to wait for 20 years to expire.

Companies are required to have certain records **available for inspection** at a certain place and at specified times. In addition to keeping these documents at the registered office, the Government proposes to allow companies to keep them in one other **location**. This means that small companies which do not necessarily have a registered office that can be open to shareholders and others for documents to be inspected as required will still be able to keep their records in another place, e.g. at their solicitors' offices. The alternative venue will have to be stated in the annual return, annual accounts and reports, any website and on request.

In addition, the Government proposes that private companies should only be obliged to make their records available for inspection for at least 2 hours between 9am and 5pm on business days during the notice period for a general meeting. At other **times**, the records will have to be made available for at least 2 hours on request. Public companies will, however, still have to make their records available for at least 2 hours between 9am and 5pm on business days.

Companies House

See CLM: ¶4027+, ¶4030, ¶4048, ¶4049, ¶4076, ¶4080

Companies House will be able to **annotate the register** under the new Act. During the transitional phase, the Government has stated that this power will be used to clarify any discrepancies which arise as a result of different filing requirements under the old and new regimes. Once the Act is in force, the Government has proposed that Companies House should be able to exercise this power to explain any material on the register which may be confusing or misleading to a person searching it.

Companies House will also have the power to **remove information from the register**. The current proposals for the type of material that will be able to be removed are restricted to material which could be used to commit fraud (e.g. in the case of a hijacked company, where fake documents are filed by criminals who then use the company to commit fraud). Such material will be able to be removed from the register on the application of a person affected by the document.

Provisions enabling regulations to be made allowing certain documents to be **filed in another language**, with English translations, are already in force. The Government proposes to allow overseas companies who have a presence in the UK to file their memoranda and articles in a foreign language with a translation as well.

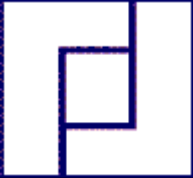
Certain company documents have to be **advertised in the Gazette** at the moment. The new Act will enable regulations to be made giving Companies House the power to require that this information is published in an alternative manner. However, the Government has stated that it does not propose to use this power at this stage.

Company secretaries

See CLM: ¶4129

Many private companies are likely to take advantage of the removal of the requirement to have a company secretary under the new Act. In order to prevent confusion arising over the status and powers of former private company secretaries, the Government is proposing to put transitional arrangements in place to clarify the position where a private company has decided not to have a secretary, but has not filed Form 288b to remove him from the register at Companies House.

CA 2006



COMPANIES ACT 2006: IMPLEMENTATION cont...

Company accounts

See CLM: ¶4226, ¶4303, ¶4369

Under the new Act, the detailed accounting and reporting requirements will be set out in regulations. The Government has announced its proposals regarding these regulations. In line with its “think small first” approach, it proposes introducing a single set of regulations for **small companies**. It is considering whether the same regulations should also apply to those small companies which are parent companies and which choose to prepare group accounts. For **medium-sized and large companies**, the Government has yet to decide between one set of regulations for them all, or taking an alternative approach.

The Government has confirmed, however, that in most respects, the new regulations will not change the substance of the current requirements. However, it does propose to make some **policy changes** in the following areas:

- » further reporting requirements relating to the way in which companies take pay and employment conditions elsewhere in its group into account in deciding directors’ remuneration;
- » a new requirement for small and medium-sized companies to disclose turnover in their abbreviated accounts; and
- » the threshold for the disclosure of charitable and political donations to be raised from £200 to £2,000.

For the first time in legislation, the new Act sets out how **auditors** may limit their liability for their audit of company accounts. The Government has announced that it does not intend to prescribe or proscribe the terms of **liability limitation agreements** unless, against its expectations, the freedom for companies and auditors to choose the terms themselves results in adverse effects, for example on competition.

However, such agreements will have to be disclosed and the Government will be making regulations that will specify the **content and method of disclosure**. It proposes that the information to be disclosed will be the principal terms of the agreement and the date of the shareholders’ resolution which approved the agreement, or waived the need for approval. The method of disclosure will be by means of a note to the annual accounts.

Derivative claims

See CLM: ¶7130

The Government proposes to allow shareholders who bring a derivative claim on or after the commencement date for the relevant provisions (October 2007) to use the new procedure, whether or not the actions or omissions complained of took place before that date.

▶ Contents

▶ News

▶ Cases

▶ Legislation

▶ Focus on...

▶ CA 2006

▷ All newsletters

▷ Online updates

▷ Email us



PDF printer
friendly version

CA 2006