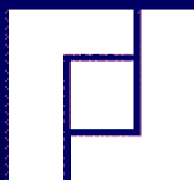

COMPANY LAW MEMO 2007

Newsletter Issue 3 **May 2007**

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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.

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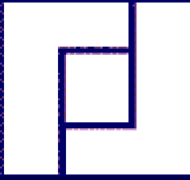

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Consultation: IoD guidance for boards on health and safety at work

See CLM: ¶2590

At the request of the Health and Safety Commission, the Institute of Directors (IoD) is **consulting on** a new draft of its **guidance** for boards on the issue of health and safety good practice.

The draft guidance sets out four core actions to be taken along with good practice guidelines on how these actions should be effected. The actions are:

» **Planning**: this involves complying with the legal requirement for companies with more than five employees to have a written health and safety policy, as well as ensuring that health and safety is a core part of the company's culture, values and performance standards, e.g. having in place effective strategies for communication about health and safety within the company, a regular review procedure, allocating responsibility for health and safety matters and making sure that the issue is regularly addressed by the board.

» **Delivering**: by putting the appropriate management systems and practices into place. This includes ensuring that adequate resources are devoted to the issue and that risk assessments are carried out.

» **Monitoring**: both incident-led and routine reporting need to form part of a company's monitoring strategy. Companies need to review changes in work practices and procedures to make sure that health and safety issues continue to be addressed, as well as investigating major failures. Companies also need to keep up to date with developments in health and safety regulation and adapt their policies and practices as necessary.

» **Reviewing**: health and safety performance should be reviewed by the board on an annual basis (as a minimum).

The draft guidance stresses the **benefits** to businesses of dealing with health and safety issues properly, including reducing costs by minimising employee absences and potential legal actions, and improving the company's reputation. It also reminds directors and other officers of their potential personal **liability** for health and safety breaches, and the fact that directors can be disqualified for conviction of this offence as well (see CLM ¶3012).

The draft guidance is available on the IoD website: *www.iod.com*. **Responses** on the content and accessibility of the draft guidance are invited to be submitted by 22 June 2007. The IoD proposes to issue a version suitable for smaller companies in due course.

Consultation: Implementation of new penalties for employing illegal migrant workers

See CLM: ¶2598

The Home Office's Border and Immigration Agency has issued a consultation document dealing with the implementation of the measures to prevent illegal migrant working contained in the new Immigration, Asylum and Nationality Act 2006 (which is not yet fully in force).

If a company employs a person over 16 who does not have permission to live and work in the UK, it will be liable to a **civil penalty** (s 15 Immigration, Asylum and Nationality Act 2006). The consultation states that employers who employ illegal migrant workers because of negligent recruitment and employment practices will find themselves subject to this penalty. One of the questions the consultation asks is whether the maximum fine should be £5,000 or £10,000.

There will be a separate **criminal offence** of knowingly employing illegal migrant workers, which could result in a prison sentence of up to 14 years and/or an unlimited fine (s 21 Immigration, Asylum and Nationality Act 2006). Directors may be personally prosecuted for this offence (s 22 Immigration, Asylum and Nationality Act 2006).

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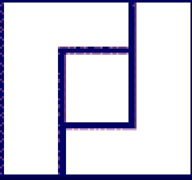

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The consultation document sets out the **range of enforcement action** which can be taken against employers for breach of the requirements, ranging from making educational visits to an employer to assist it to comply with the law and drawing up an action plan, through liability for the civil penalty, to prosecution for increasingly severe commissions of the criminal offence. The consultation also sets out a draft code of practice which will be applied in deciding on the level of civil penalty that should be awarded in different circumstances.

Guidance for employers on the changes to the law on preventing illegal working will be available before the new Act is implemented.

The consultation document can be found at: *www.bia.homeoffice.gov.uk/lawandpolicy/consultationdocuments*.

Responses are invited by 7 August 2007.

Corporate Manslaughter Bill: the debate continues

See CLM: ¶2591, ¶7178

The Corporate Manslaughter and Corporate Homicide Bill has reached the "ping pong" stage of its passage through Parliament. As reported in *Issue 1*, the House of Lords had introduced amendments into the Bill so that the offence covered deaths in custody. The House of Commons rejected these amendments, proposing instead that the Bill should include a power for the secretary of state to extend the definition of "duty of care" to include duties owed under negligence law to those in custody. This would have left the possibility of extending the new Act open, without actually committing to it at this stage. The House of Lords considered and rejected this proposal on 22 May, insisting on its original amendments "because it is appropriate that a relevant duty of care should be owed to anyone held in custody". Judging by the Commons' published response to this on 24 May, which puts forward another provision containing the same power, the two Houses are currently deadlocked.

For a discussion of the Bill, see *Issue 1*. Readers can follow the progress of the Bill at: *http://www.publications.parliament.uk/pa/pabills.htm*.

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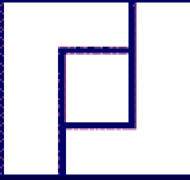

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Case law

Application to set aside disqualification undertaking following breach of director's right to a fair trial

See CLM: ¶3072, ¶7393+

Eastaway v Secretary of State for Trade and Industry [2007] EWCA Civ 425

Disqualification **proceedings** were **commenced** against Mr E, a tax and accountancy professional who was a director of companies in the B group, in 1992. Mr E defended the proceedings and sought judicial review of the secretary of state's decision to make the disqualification application. When making the order adjourning the disqualification proceedings pending the judicial review, the judge required Mr E to agree to give a disqualification undertaking if his judicial review application was unsuccessful. The application for judicial review failed. Mr E then applied for the disqualification proceedings to be dismissed on the basis that the proceedings had taken an excessive length of time. At a hearing in 2001, the judge rejected the application. Mr E applied for permission to appeal this decision, and was refused twice. The disqualification proceedings were stayed in May 2001 to allow Mr E to enter into a **disqualification undertaking** for 4 1/2 years.

Mr E then applied to the **European Court of Human Rights** (ECHR) for relief on the basis that the disqualification proceedings violated his right to a fair trial because they had taken too long (art 6 European Convention on Human Rights). In July 2004, the ECHR upheld his complaint and awarded him compensation for his legal costs in establishing the violation. Mr E then **applied** to have the **undertaking set aside** on the basis that the ECHR's finding meant that there could not have been a fair trial. Although the undertaking expired on 31 December 2005, Mr E argued that it continued to prejudice him in his career because the professional bodies of which he was a member would institute disciplinary proceedings against him if the undertaking was not set aside.

The Court of Appeal **rejected** his **application** for a number of reasons, which can be summarised as follows:

- the ECHR found that Mr E's right to a fair trial had been violated because of the length of time that the proceedings had taken. It did not find, and it could not be implied, that there could have been no fair trial of the disqualification application despite the delay (*Attorney General's Reference (No 2 of 2001)* [2004] 2 AC 72);
- at the 2001 hearing of Mr E's application to dismiss the disqualification application, he did not contend that a fair trial was not possible because of the length of the proceedings. There was no evidence that a fair trial would not have been possible in May 2001 when Mr E gave the undertaking. In any event, any such breach of Mr E's convention rights was waived by him when he gave the undertaking and there were no public interest reasons on the facts of the case to prevent the waiver;
- Mr E was represented throughout the proceedings by solicitors and sometimes by counsel as well. He understood the effect of the undertaking and was not forced to give it. He benefited from it by avoiding the cost and publicity of a trial; and
- Mr E had not given sufficient evidence to show that the length of time the proceedings had taken (as opposed to the fact that he was disqualified, which will inevitably prejudice a professional person) had caused him substantial enough prejudice to warrant dismissing the proceedings. Whether his professional bodies thought that disciplinary proceedings were necessary was for them to decide, looking at the reasons for Mr E's disqualification. It was not a matter for the court to consider.

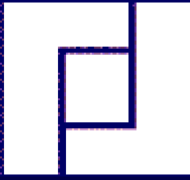
The Court of Appeal also stated that the **court's power** to set aside a disqualification undertaking is not contained in r 7.47(1) IR 1986, as this only applies to orders made in the court's exercise of its insolvency jurisdiction.

Parent company guarantee

See CLM: ¶4696, ¶5469, ¶ 6603

Wolsey Securities Ltd v Abbeygate Management Services Ltd [2007] EWCA Civ 423

The Court of Appeal has decided that a parent company guarantee in a joint venture agreement (JVA) covered payments due under a separate facility letter.



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The judges were unanimous in holding that whether the JVA and facility letter formed a single or separate agreement was immaterial. Since the facility letter was referred to in the JVA, both had to be interpreted in light of the other. On the drafting of the documents before them, the judges declared that the guarantee in the JVA did cover some of the charges due under the facility letter. This decision overturns Park J's decision in the High Court ([2006] EWHC 1493 (QB), see *CLM Newsletter July 2006*). However, it is not a complete victory for the claimant as some of the charges due under the facility letter were excluded from the guarantee. The case therefore still highlights the importance of drafting parent company guarantees to cover all potential payments.

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Financial assistance – Loan to repay indebtedness

See CLM: ¶5572, ¶5631+

Anglo Petroleum Ltd v TFB (Mortgages) Ltd [2007] EWCA Civ 456

The Court of Appeal has confirmed that:

- a good faith restructuring and repayment of indebtedness does not constitute financial assistance; and
- even if it did, a lender who loaned the money to make the repayment would still be able to enforce the terms of its loan agreement (and any related guarantee and security).

In this case, an unsecured inter-company loan between AP Ltd and its parent was restructured as part of the sale of AP Ltd's entire issued share capital. The terms of the restructuring reduced AP Ltd's indebtedness by £30 million and in return AP Ltd gave security to the parent for repayment of the remaining £15 million.

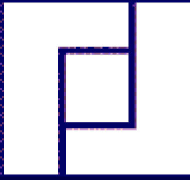
The Court held that just because the restructuring made AP Ltd a more attractive target and smoothed the path to the acquisition, it did not follow that this amounted to financial assistance. The restructuring had been carried out in good faith. The reason for it was to sell AP Ltd's shares but that did not make the purpose that of giving financial assistance to the buyer.

Three months after the sale, AP Ltd took out a loan from TFB Ltd at a high rate of interest to repay the indebtedness earlier than required. The Court confirmed that the repayment of lawful indebtedness is not financial assistance. The Court also decided that the high cost of the borrowing, which reduced AP Ltd's assets, did not convert the repayment into unlawful financial assistance. However, the Court accepted that in some cases the early repayment of indebtedness so as to benefit the buyer could amount to financial assistance. In this case, the Court accepted that there were good faith reasons why AP Ltd wanted to repay early (so that it and the buyer could obtain further finance at favourable rates).

The Court then considered whether the loan by TFB Ltd would have amounted to an illegal contract if financial assistance had occurred. In this case, TFB Ltd knew that the loan would be used to repay the restructured indebtedness.

The Court found that the terms of the loan did not require AP Ltd to act illegally. TFB Ltd was therefore entitled to assume that it would use the funds without breaking the law. The fact that TFB Ltd knew of AP Ltd's unlawful purpose (assuming that the repayment would have been unlawful financial assistance) was not sufficient; "active participation" on the part of TFB Ltd was required. What amounts to active participation varies from case to case keeping in mind the public policy basis of the law in this area. Here, the Court decided that it would not be in the interests of public policy to invalidate a contract which was not unlawful in its terms and which a reasonable person in TFB Ltd's position would have seen as an ordinary innocuous commercial transaction. The principle that ignorance of the law is no defence did not stretch that far.

This decision upholds the order of Peter Smith J in the High Court ([2006] EWHC 258 (Ch)).



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The final **text** of the Companies Act 2006, explanatory **notes and tables** of destinations and origins are now freely available to download at: *http://www.opsi.gov.uk/acts/acts2006a.htm*

The Act received Royal Assent on 8 November 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.

Various provisions of the new Act **came into force on 6 April 2007**. These were discussed in *Issue 2*.

The Government is currently **consulting** on some secondary legislation and transitional arrangements: see *Issue 1* for details.

Also see *Company Law Memo 2006 Newsletter Issue 9* for a summary of ICSA's guidance on the new **company communication provisions** which came into force in January 2007.

The Government has published three **new** sets of **draft regulations** this month, which are discussed below. These are in addition to the draft regulations exempting certain types of company from having to obtain shareholder approval for "political" expenditure (see *Issue 2*). The Government expects to be able to publish a draft of the next Commencement Order in June (which will bring into force the next tranche of provisions of the Act in October), and hopes to have drafted all of the secondary legislation to the new Act by the end of this year.

Company formation

See CLM: ¶394+, ¶519, ¶526, ¶527, ¶660, ¶682

The draft Companies (Registration) Regulations 2007 set out the **new form of memorandum** that will be required of companies incorporating under the Companies Act 2006 (reg 2, Sch 1, Sch 2). This is a very simple statement that the subscribers wish to form a company, that they agree to become members and, in the case of companies with a share capital, that they agree to take at least one share each. There are separate memoranda for companies with share capital and those without.

As part of the incorporation process under the new Act, companies with share capital will have to include a **statement of capital and initial shareholdings** in their application for registration. The same draft regulations require this statement to include the names and addresses of the subscribers (reg 3). Likewise, for companies limited by guarantee, the **statement of guarantee** will have to include the names and addresses of the subscribers (reg 4).

These draft regulations also set out the form of assent required from the shareholders to **re-register** a public or a private limited company **as an unlimited company** (regs 5, 6, Sch 3, Sch 4).

The draft Companies (Registration) Regulations 2007 will come into force in their final form on 1 October 2008, along with the incorporation provisions of the new Act.

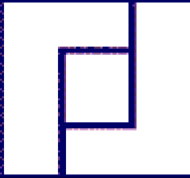
Shares and share capital

See CLM: ¶374, ¶526, ¶685, ¶715, ¶915, ¶1087, ¶1318, ¶1325, ¶1326, ¶1378, ¶1394, ¶1404+, ¶1428, ¶1469, ¶1489, ¶1493, ¶1612, ¶1828, ¶4062

The draft Companies (Shares, Share Capital and Authorised Minimum) Regulations 2007 deal with various details to do with shares and share capital which were not addressed in the new Act.

» The draft regulations set the euro equivalent of the **minimum allotted share capital** for public companies at €75,000 (reg 2). This is an alternative to the sterling figure of £50,000.

» If a public company's minimum allotted share capital is in a currency other than sterling or euros, the draft regulations set out how the authorised minimum figure is to be calculated where the company's share capital has been reduced to determine whether or not the company still meets the minimum requirement (reg 3).



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» If a public company has used the new redenomination procedure with the effect that its share capital is reduced below the minimum allotted share capital level, the draft regulations require it to re-register as a private company within a year and set out a procedure for doing so (regs 4-8).

» The new Act prohibits the distribution of **reserves resulting from a reduction of share capital**. However, the draft regulations create an exemption for the following types of reduction (reg 9):

- reductions confirmed by the court;
- reductions made out of court supported by a solvency statement, to the extent that the reserve is treated as realised profit; and
- any reduction carried out by an unlimited company.

» The draft regulations enable reserves resulting from a reduction of share capital to be treated as realised profit except in certain situations (reg 9):

- where the company is unlimited and its articles provide that such a reserve cannot be treated as realised profit;
- where the reduction of capital is approved by the court and the court orders that the reserve cannot be treated as realised profit; or
- where the reduction is made out of court supported by a solvency statement, but only to the extent that the reserve is not treated as realised profit.

» The draft regulations require a solvency statement in support of an out of court reduction of capital to be in writing, state that it is a solvency statement and be signed by each director (reg 13).

» They also require a directors' statement regarding the **payment out of capital** by a company for the **redemption or purchase of its own shares** to be in writing, state that it is a directors' statement, state whether the company's business includes that of a banking or insurance company and be signed by each director (reg 14).

» A number of filing obligations under the new Act require a company to provide a "**statement of capital**" to Companies House. The draft regulations set out the contents of such a statement as follows (reg 10):

- rights to vote at general meetings, including those which are limited to certain circumstances;
- rights to dividends;
- rights to participate in a distribution of capital, including on a winding up; and
- whether the shares will be redeemed, or can be redeemed at the option of the company or the shareholder, and any terms of that redemption.

» The draft regulations also set out the information that will be needed to complete a **return of allotment**:(reg 11):

- the number of shares allotted;
- how much is paid up and how much is not (including of any premium as well as the nominal value of the shares); and
- if the shares have not been paid up (fully or partly) in cash, what the consideration was.

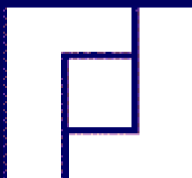
» The draft regulations also allow payment for shares using **CREST** to be regarded as cash consideration (reg 12).

The draft Companies (Shares, Share Capital and Authorised Minimum) Regulations 2007 will come into force in their final form on 1 October 2008.

Company management - access to company records

See CLM: ¶2044, ¶2513, ¶2669, ¶3869, ¶3930, ¶3994

The draft Companies (Fees for Inspection and Copying of Company Records) Regulations 2007 will replace the current **fees** companies can charge to comply with requests to **inspect and copy** certain registers and other records kept by the company (these are currently set out in SI 1991/1998):



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- register of shareholders:
  - fee to inspect: £3.50 per hour
  - fee to provide copies: £3.50 for the first 50 entries, £31.50 for the next 950 entries, £20 for the next 4,000 entries, and £25 for every subsequent 5,000 entries;
- fee to inspect the Index of shareholders' names: £3.50 per hour;
- fee to provide copies of the register of interests in shares: £3.50 for the first 50 entries, £31.50 for the next 950 entries, £20 for the next 4,000 entries, and £25 for every subsequent 5,000 entries;
- fee to provide copies of a director's service contract or memorandum of terms: 20p for every 1,000 words;
- fee to provide copies of a director's qualifying indemnity provision: 20p for every 1,000 words;
- fee to provide copies of records of resolutions and meetings: 20p for every 1,000 words; and
- fee to provide copies of reports on interests in shares: 20p for every 1,000 words.

These fees are intended to allow companies to recover their costs of meeting their statutory obligations without discouraging shareholders and others from exercising their rights to access these records.

The draft Companies (Fees for Inspection and Copying of Company Records) Regulations 2007 will come into force in their final form on 1 October 2007.

The regulatory impact assessment published with these draft regulations includes a useful table summarising how statutory rights of access will change under the new Act.

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