

Companies Act 2006: implementation

Introduction

This bulletin follows our previous article published in July 2007 and addresses three issues concerning the prospective implementation of the Companies Act 2006 which are of general application.

Commencement Order Number 3

The Government has now reissued the Number 3 Commencement Order following its withdrawal in July as a result of errors in the documentation. The document is approximately 80 pages long and contains provisions for the implementation with effect from 1 October 2007 of a number of provisions as mentioned in our previous article, including:-

1. Section 170 to 181 (the general duties of directors) other than in respect of those aspects concerning conflicts of interest, and
2. Transactions with directors requiring the approval of members (Sections 188 to 226). It should be noted that this replaces the existing provisions concerning:-
 - (a) Service contracts - two year maximum rather than five,
 - (b) Property transactions,
 - (c) Loans to directors – which will now require members' approval rather than being illegal,
 - (d) Payments for loss of office and payments in connection with the transfer of an undertaking, and
 - (e) Provisions protecting directors from liability.

Model Articles of Association

The Secretary of State has published Regulations containing draft Articles of Association for private companies limited by shares, private companies limited by guarantee and public companies. These will not affect the companies which choose not to adopt them or which are already in existence. The Regulations are to come into force on 1 October 2008.

Of particular interest are the provisions of Schedule 1 which set out model Articles for private companies. They are structured entirely differently from the historic version and begin by addressing the responsibilities and powers of directors.

They also contain a number of new provisions, but do not contain provisions for alternate directors.

There are new rules for decisions taken by shareholders including specific rules regarding the amendment to Resolutions at General Meetings and the ability of the Chairman to invite non-members or non-officers to address a meeting.

Business Review

There has been widespread press comment on the obligations which directors will incur under the statutory duties provisions as referred to in our previous article, which come into force on 1 October 2007.

There has been less comment on the provisions of Section 417, which also comes into force on 1 October 2007 in line with the provisions regarding the directors' duties themselves.

With the exception of companies which are subject to the small companies regime (set out in Section 382), directors' reports must contain a business review. The purpose of the business review is to inform members and help them assess how the directors have performed their duty under Section 172 (duty to promote the success of the company).

The review must contain:-

- (a) A fair review of the company's business, and
- (b) A description of the principal risks and uncertainties,

The review required is a balanced and comprehensive analysis of:-

- (a) The development and performance of the company's business during the financial year, and
- (b) The position of the company's business at the end of the year consistent with the size and complexity of the business.

Quoted companies will need to set out in their business review further information concerning main trends and factors and

information about environmental matters, the company's employees and social and community issues.

Although there are certain exclusions in relation to non-financial information for medium sized companies (for a definition of which see Section 465 to 467) all companies that are obliged to make a review must comply with the following:-

"The review must, to the extent necessary for an understanding of the development, performance or position of the company's business, include:-

- (a) Analysis using financial key performance indicators, and
- (b) Where appropriate analysis using other key performance indicators, including information relating to environmental matters and employee matters."

"Key performance indicators' mean factors by reference to which the development, performance or position of the company's business can be measured effectively."

Although it is not specifically stated, it would appear that medium sized companies only have to comply with (a) immediately above rather than both (a) and (b).

The review must, where appropriate, include references to any additional explanations of amounts included in the company's annual accounts.

There are savings in relation to the disclosure of information if it is in the opinion of the directors seriously prejudicial to the interests of the company. The saving in this connection relates to information about impending developments or matters in the course of negotiation. There is also a public interest exclusion.

It is essential that directors of companies are aware that, not only must they be seen to be following best practice in relation to acting as a director, but they must positively analyse how they have done so in relation to any company obliged to produce a business review.

These provisions affect everyone other than those who are directors only of companies which qualify as "small" companies.

In order to qualify as a small company, the company in the year to which the review relates must satisfy two or more of the following requirements:-

1. Turnover of not more than £5.6 million,
2. A balance sheet total of not more than £2.8 million, and
3. Not more than 50 employees.

Directors should note that, under Section 303(1), a parent company qualifies as a small company in relation to a financial year only if the group headed by it qualifies as a small group.

A group qualifies as a small group if it satisfies two or more of the following:-

1. Aggregate turnover of not more than £5.6 million net (or £6.72 million gross),
2. Aggregate balance sheet total of not more than £2.8 million net (or £3.36 million gross), and
3. Aggregate number of employees of no more than 50 employees.

"Net" means after set offs and adjustments made to eliminate group transactions.

It is therefore essential that directors of companies are aware of their obligation positively to review their performance in the light of their obligations to comply with the provisions in the Companies Act 2006 regarding directors' duties.

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