ORGANISATION DE COOPÉRATION ET DE DÉVELOPPEMENT ÉCONOMIQUES

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ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

The UK's Company Law Review

Submitted by

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Company Law Reform in OECD Countries
A Comparative Outlook of Current Trends

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In the Spring of 1998 the UK launched a major three year Company Law Review. The Review has been managed by an independent Steering Group, and has proceeded on a very open and consultative basis; its final report is expected in May 2001.

On 30 November the Review published its latest major consultation document. The executive summary is attached, and the full text may be found on the internet at: http://www.dti.gov.uk/cld/reviews/condocs.htm, where the other seven consultation documents from the Review may also be found.

Jonathan Rickford, the Project Director for the Review, will be speaking at the second Panel session on 7 December.

4 December 2000

EXECUTIVE SUMMARY

1 This consultation document takes forward the proposals on which we consulted in *Developing the Framework,* revising them in the light of responses and inviting further comments on a limited number of issues which emerged from the consultation. It also sets out proposals in areas not previously addressed in consultation, where views are sought across a broader range of issues.

Chapter 2

2 Chapter 2 addresses the needs of small and private companies. It covers three areas:

- the need to make the law accessible to all who use it, particularly those involved with small companies;

- the specific proposals to simplify the company law and accounting requirements for private companies put forward in *Developing the Framework*; there was a large measure of support for these proposals and we intend to proceed with them; we invite views on some detailed points, which emerged during consultation; the position of sole directors with potential conflicts of interest; the model constitution; the timetable for filing accounts and for laying them in general meetings; and the proposal for an Independent Professional Review to replace audit for certain private companies (broadly speaking, those with a turnover of between £1 million and £4.8 million); and

- on the distinction between private and public companies; we invite views on the restrictions in section 81 on private companies offering their shares to the public, and the scope for alignment with the Public Offer of Securities Regulations.

Chapter 3

3 This chapter largely confirms the position on "scope" as set out in *Developing the Framework*, in particular the proposals for an inclusive statement of directors' duties (i.e. one which would require directors to promote the success of the company in the interests of its members, but taking account of all relevant considerations, including the implications for the company of their decisions over time and of wider relationships, such as those with employees, suppliers, customers and the wider community); and for improved transparency, principally through the proposed Operating and Financial Review (OFR) to be prepared by public companies and large private companies. We invite views on points arising over directors' conflicts of interest and on a proposal to strengthen the OFR by requiring the process followed in its preparation to be audited.

Chapter 4

4 The proposals in *Developing the Framework* in relation to directors and the rules in Part X of the Act on enforcement of fair dealing by directors were largely supported in responses and we confirm them here. There was little support for change on the Combined Code, and no change is proposed in this area at this stage except on payments on loss of office and some greater transparency in relation to non-executive directors and employment contracts.

5 As foreshadowed in *Developing the Framework*, we have examined in more detail the issue of companies' and directors' liability to third parties. We make proposals on a company's vicarious liability and contributory fault for frauds committed by directors in the course of their authority. We suggest that the DTI should discuss with the Lord Chancellor's Department and the Scottish Executive the scope for a general provision ensuring that the law applies effectively to all employers and principals in such cases (whether corporate bodies or not).

6 We also invite views on possible requirements where conflicts of interest may inhibit institutional investors exercising their corporate governance role.

Chapter 5

7 This chapter addresses the role of shareholders. It confirms the proposals in Chapter 4 of *Developing the Framework* and develops further the proposals on the rights of minority shareholders and the limits on the power of the majority. It proposes that: all members should have a personal right to enforce any obligation under the constitution; the unfair prejudice remedy should remain subject to the focus laid down in *O'Neill v Phillips*; derivative actions should be put on a statutory basis, extending only to breach of duty by a director, and capable of being blocked by ratification; and subject to those provisions the powers of the majority should be constrained: (i) by the requirement that decisions should be taken *bona fide* in the best interest of the members as a whole, in cases of alteration of the constitution or of class rights; and (ii) in all cases, by the disqualification of those seeking to ratify or otherwise prevent the pursuit of their own wrong or a wrong done by a person to whose influence they are subject.

Chapter 6

8 In the light of responses to *Developing the Framework* we put forward significantly revised proposals in relation to the financial reporting documents to be prepared by companies and the timetable for their publication. In particular we propose that quoted companies should publish their full annual report on their website as soon as it is available and, at the latest, within 90 days of the year end; at least 15 days must then elapse before the notice of the AGM is circulated to shareholders, to facilitate the tabling of shareholder resolutions; the accounts should be laid before the AGM and filed within 150 days; and quoted companies should continue to be able to offer Summary Financial Statements (SFS) as an alternative to the full annual report. The proposal for the preliminary announcement to be circulated to all shareholders has been dropped, but the requirement for it to be published on the company's website is retained. The proposals for other public companies are also revised in view of the changes for quoted companies.

9 The proposals in *Developing the Framework* for greater delegation of detailed accounting requirements to a standards-setting body were broadly welcomed, and we confirm them here. A number of further important points are raised on the proposals relating to audit and auditors' liability; in particular it is proposed that, if the range of the duty of care of auditors is to be extended to potential investors and creditors, the duty of the company and its directors should be similarly extended, but that claimants should be required to prove that they have taken all reasonable steps to protect themselves from loss.

Chapter 7

10 The capital maintenance proposals have already been the subject of extensive consultation. We set out briefly the way forward on the issues proposed in the consultation document *Capital Maintenance: Other Issues*, published in June 2000. The main point is that we do not now propose to proceed with no par value shares for private companies, given that EU directive constraints preclude a similar step for public companies.

Chapter 8

11 We address here responses on companies' other disclosure obligations. We propose that the DTI and Companies House should explore the scope for enabling directors to put a "service address" on the public record, with their residential address being available only to certain regulatory and enforcement agencies, or on the order of the court. We confirm proposals to restrict the use which can be made of companies' registers of members. We propose that companies should be allowed to set a "record date" for the purposes of determining who is entitled to receive notice of meetings or to attend and vote. We confirm proposals to control company names which are misleading or registered for an improper purpose, and to simplify procedures for restoring dissolved companies to the register.

Chapter 9

12 We confirm our support for a separate form of incorporation designed for charities, to be taken forward by the Charity Commission. A similar proposal is being considered for Scottish charities by an independent Scottish Charity Law Review Commission.

Chapter 10

13 On groups of companies, we invite views on a proposal for an optional regime which would provide less onerous reporting and auditing requirements for subsidiary companies where the parent guarantees their liabilities. We also invite views on whether the prohibition on a subsidiary holding shares in its parent should be extended to apply to entities other than bodies corporate (e.g. certain kinds of partnership) over which the parent has control.

Chapter 11

14 We examine the scope for streamlining the ways in which companies can restructure, provided for in section 425 and sections 428 to 430 of the Companies Act, and section 110 of the Insolvency Act 1986. We make proposals for: a simpler statutory merger procedure within wholly-owned groups of companies; and for "jurisdictional migration", to enable companies to change their place of incorporation (i.e. to migrate into or out of Great Britain or to move between England and Wales and Scotland) without winding up and re-incorporation.

Chapter 12

15 This chapter proposes a new institutional structure to underpin a new Act; examines the areas to be devolved to a rule-making body; and, considers how the law can best be kept up to date and the best mechanism for ensuring proper consideration of secondary legislative and rule-making powers.

16 A Companies Commission is proposed, with continuing oversight of developments in company law, and with a duty to prepare an annual report on the state of company law and to advise on proposals for new legislation (including secondary legislation) and on other topics referred to it by Ministers. Subsidiary bodies would be responsible for: setting detailed rules on both accounting and reporting and other areas delegated to it (such as rules on the conduct of AGMs or corporate governance codes); enforcing reporting and accounting requirements; and ensuring that due account is taken of the needs and concerns of private companies. There are also proposals for a specialist tribunal to hear cases brought by the enforcement body.

Chapter 13

17 This chapter sets out criteria for a coherent framework of criminal and civil sanctions: considers other ways to encourage compliance, such as warning letters and reminders, and extra-legal remedies such as "naming and shaming"; suggests improvements to a number of specific sanctions; and invites views on detailed proposals for codifying civil remedies for breach of directors' duties, based on the personal remedies available under section 322. Finally it considers ways of strengthening the protection against "phoenix companies" where directors of a failed company mislead the market into believing that it is continuing to trade, or alternatively where they mislead the market into believing that a successor company is unrelated to a previous company whose debts have been abandoned.