Companies Act 2006
Implications for a Company’s Constitution

SLAUGHTER AND MAY
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COMPANIES ACT 2006
IMPLICATIONS FOR A COMPANY’S CONSTITUTION

The Companies Act 2006 will have a profound effect on the constitutions of companies, both those incorporated under the new Act and those which are already in existence. In particular, a company’s memorandum of association will cease to be part of its constitution and will merely contain limited information regarding the founders of the company. Other changes brought about by the Act will affect the provisions which companies have in their articles of association.

The Government is preparing new model form articles which will replace the old Table A. There will be separate model articles for public and private companies.

Existing companies will need to be aware of transitional provisions which will automatically alter their memorandum and articles of association, and consider when and how to make amendments to bring their constitution into line with the new law.

When should companies amend their constitution?

Background

The question of when a company should amend its constitution has to be looked at in the context of three issues. The first of these is the Government consultation process. Comments on the latest drafts of the model form articles were requested by the end of May, and it is hoped that the drafts will be in reasonably final form by October of this year. The model forms will then be a backdrop against which a company can consider changes to its own constitution. The Government is also consulting on transitional provisions and is more or less committed to completing this by the end of this year. These provisions need to be in place before a company can finalise its own proposals to change its constitution.

The second issue is the desirability of a dialogue between lawyers and with companies, in particular in relation to some of the more difficult issues such as directors’ duties, to ensure some degree of consistency in how companies propose to deal with the changes. This should proceed during the remainder of this year in tandem with the Government consultation process.

The final piece of the jigsaw is the effect of the timetable for implementation of the Act. The Government has been relatively accommodating in the timing of changes which affect companies’ constitutions. These changes will generally not come into force until October 2008 so as to allow for consultation during the course of this year and for companies to prepare themselves to make amendments to their constitutions in the following year.

Public companies

Public companies, and particularly quoted companies, will want to avoid having to convene an extraordinary general meeting to make changes to their constitution. Against the timing backdrop discussed above, it is hoped that companies and their advisers will have relatively firm proposals by the end of this year for the changes they wish to make, and the conclusion therefore is that public quoted companies should look at changing their articles during the 2008 AGM season. This also appears to be what the Government is anticipating.
Quoted companies will need to prepare circulars to their shareholders describing the changes they want to make to their constitution. Such circulars would need to be approved by the UKLA if the changes had “unusual features”. All companies are likely to be making similar, if not the same, changes to deal with the new Act and the UKLA has indicated that its inclination is that it will not want to vet these circulars. It is proposed that, once the basis of amendments has been finalised, a pro forma circular be submitted to the UKLA to enable it to determine the need for approval or otherwise.

The views of the investment committees of the ABI and NAPF should also be sought in relation to certain of the changes which companies are likely to make, in particular the basis on which directors’ duties are to be dealt with. This opportunity should also be taken to persuade the ABI that borrowing limits should be removed from articles of association, given that they serve little real purpose.

As companies will be holding AGMs prior to 1 October 2008 when the final parts of the new Act come into force, the resolution which companies pass to amend their articles will need to be drafted so as to take effect on 1 October 2008. The resolution and amended articles of association will need to be filed at Companies House within 15 days of the resolution being passed even though the effective date of the changes is likely to be later.

Different timing issues arise for companies incorporated before the Act comes fully into force, which will need to consider how to draft their articles to straddle the old and new regimes.

There are a number of areas where companies’ current constitutions are likely to contradict provisions of the Act which come into force before 1 October 2008. A good example is in relation to shareholder meetings, where a number of changes are made in the Act to enfranchise proxies. Most companies’ constitutions will provide that proxies cannot vote on a show of hands and that a corporate shareholder cannot appoint multiple corporate representatives. This is in line with the current law and practice. However, provisions in the Companies Act 2006 which come into force in October this year will liberalise this area. Fortunately, these provisions are free standing and do not require changes to a company’s constitution in order to take effect. They simply provide that, to the extent that the constitution says otherwise, the Act will prevail.

Private companies

The situation for private companies is slightly different from that for public companies, as there is more deregulation in the new Act for private companies and this deregulation is being implemented in stages. For example, from October 2007 the default position for a private company will be that it does not need to hold AGMs. However transitional provisions are likely to provide that, if an existing company has express provisions for an AGM in its articles, these will continue to have effect. Also from October 2007, the shareholders of a private company will be able to pass a written resolution without a requirement for unanimity, unless this requirement is contained in its articles. With effect from April 2008, a private company will not need to have a company secretary, but if there are references in its articles that directly require or assume the requirement for a company secretary, transitional provisions are likely to provide that these should continue to have effect.
The question here is whether it is worth, in certain instances, making amendments to a private company’s articles sooner to take advantage of the deregulatory provisions as they come into force. Different sorts of companies may well take different approaches here, depending on how useful each wave of deregulation will be for that company and how easy it is to effect changes to the company’s constitution. For example, in relation to wholly owned subsidiaries, the ability to avoid multiple AGMs in 2008 may be attractive for large groups. If the resolution adopting the new articles is properly framed, it should be possible for private companies to adopt new articles earlier than public companies.

As with public companies, private companies incorporated before all the provisions come into force may need to adopt articles which straddle both the old and new regimes.

How should companies amend their constitution?

The changes which companies should consider making to their constitution can be divided into several broad categories.

First, there is a requirement to counter-act the effect of certain of the transitional provisions. For example, section 28 of the Companies Act 2006 has the effect of moving certain provisions from the memorandum of an existing company into its articles of association. One of these provisions is the clause setting out the objects of the company. New companies formed under the 2006 Act will have unrestricted objects, so there will be a distinction between existing and new companies in this respect. Many existing companies will wish to remove the objects clause from their constitution so that they too will have unrestricted objects.

If a company has provisions in its memorandum which will be transferred into the articles by section 28, and it wishes to keep these provisions going forward, it will need to check whether there is any inconsistency between these provisions and other provisions in its articles. At present, in such a situation, it is the provision in the memorandum which prevails. In future, any inconsistency would need to be resolved by the shareholders or, in the last resort, by the courts.

Another example is that the concept of authorised share capital is being abolished for new companies, while for existing companies transitional provisions are likely to provide that references to authorised share capital in constitutions of companies will continue to operate as a restriction on the shares which they can issue. This will contrast with the position for companies formed under the new Act. To ensure parity, the relevant provisions would need to be removed from the articles of existing companies. Removal will mean that consequential changes will be required to remove provisions which put unissued shares at the disposal of the directors and which enable the company to increase its share capital and cancel unissued shares, as they will no longer be necessary.

Parity with companies formed under the Companies Act 2006 is probably more of an issue for private companies than public companies, given the deregulatory nature of the Act particularly in favour of private companies. As noted above, there are areas where private companies will currently have requirements in their articles which could be removed because they are no longer necessary, for example in relation to AGMs and company secretaries, or where requirements could be relaxed such as in relation to written resolutions. Companies should look at putting themselves on an equal footing with the regime for existing companies.
Articles of both public and private companies tend to replicate a number of legislative provisions. This will be exacerbated under the Companies Act 2006, as the new Act now deals in the legislation with a number of issues that were previously dealt with in Table A. The commentary which accompanies the Government’s draft model articles indicates that they have sought in many areas to remove provisions which are covered by the Act itself, leading to simpler, shorter articles. This approach also has the advantage that, if a legal requirement in the Act changes in the future, the company will not be in the invidious position of still having to observe the old requirement because it remains in its articles as well as observing the new legal requirement.

Both public and private companies should use this opportunity to emulate this approach. Examples of relevant provisions include those dealing with notice of shareholder meetings, voting rights and the basis on which shareholders’ rights may be varied. These are all set out in the legislation and there is no need for them to be repeated in a company’s constitution.

Another area which companies should address is that of new enabling provisions introduced by the Act. This includes the ability to have a provision in articles of association enabling directors to authorise certain conflicts of interest between directors and the company. This is discussed in more detail below. Other examples are that it will be possible under the new Act to change a company’s name by resolution of the directors and for directors to fix the terms and conditions for redemption of redeemable shares, provided in each case that there is an enabling provision in the company’s constitution.

Finally, companies should consider amending their constitutions to reflect certain other changes brought into effect by the Companies Act 2006. Here, the main objective is the removal of a number of provisions that companies currently have in their articles but which will no longer be necessary. Examples in this category include authorities for a company to purchase its own shares, to reduce its share capital and to subdivide or consolidate shares. Under the Companies Act 1985, a company needs both an enabling power in its constitution and approval of shareholders before it can do any of these things. Under the Companies Act 2006 there is no longer a requirement to have an enabling provision in the articles; only shareholder approval will be necessary. Removal of these provisions will lead to further streamlining of the articles.

**Directors’ duties and the company’s constitution**

The basic prohibition in section 175 of the Companies Act 2006 is that a director must avoid a situation in which he has, or can have, a direct or indirect interest that conflicts or possibly may conflict with the interests of the company.

One important change to the current law is that this duty will no longer apply to a conflict in relation to a transaction or arrangement between a director and the company itself. It is usual for existing articles of association, of both public and private companies, to contain a list of provisions that enable directors to transact with the company in certain circumstances without being in breach of their duty to avoid conflicts. These provisions will no longer be necessary and can be removed.

It will still be good practice for a director to be prohibited from voting or counting towards the quorum when the board is considering a transaction or arrangement between him and the company, unless the transaction or arrangement benefits all the directors at the same time.
Articles will therefore continue to contain such a prohibition, together with a list of exclusions relating to matters such as taking out directors’ and officers’ liability insurance and adopting an employee share scheme.

Section 175 goes on to provide that a director’s duty to avoid conflicts is not infringed if the matter is authorised by the non-conflicted directors. For a private company incorporated under the Companies Act 2006, such authorisation can be given by the directors if the articles do not prohibit such authorisation. For a pre-existing private company, or for a public company whenever incorporated, the articles must expressly provide for the directors to be able to give such authorisation. Changes will therefore be necessary to enable directors to take advantage of this provision.

The Act provides in section 180 that, where a company’s articles contain provisions for dealing with conflicts of interest, the directors will not be in breach of duty if they do anything which is in accordance with those provisions. Companies may wish to take this opportunity to review their articles to ensure that appropriate provisions are included to benefit from this safe harbour.

The model articles

The Government is proposing separate model articles for public and for private companies. For public, particularly quoted, companies the model articles are unlikely to be something that a company would want to adopt wholesale. However, they provide a useful source of provisions and the drafting is often a simplification or amplification of the provisions which companies currently have in their articles. In that context, they should be considered when a company is considering changes to its articles. In addition, the model articles are useful in identifying provisions which are adequately covered by the Companies Act 2006 and which no longer need to be included in articles of association.

The model articles are likely to be a useful basis for private companies, with suitable adaptation for different types of private company.

Conclusions

In relation to public companies, the 2008 AGM season will be the optimal time for making amendments to the company’s constitution to deal with the Companies Act 2006. Some private companies may consider making changes earlier to take advantage of some of the deregulation which is being brought into force in advance of other provisions in the Act.

For all companies, but especially for quoted public companies, this will be a good opportunity to simplify their constitutions and to make them shorter and clearer, plain English documents which are therefore easier to use.

This briefing paper is not intended to provide legal advice, which should be sought on particular matters. Please refer to your usual contact at Slaughter and May for further information about the Companies Act 2006.

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### COMPANIES ACT 2006
### CHECKLIST OF SECTIONS AFFECTING ARTICLES OF ASSOCIATION

<table>
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<th>Section</th>
<th>Description</th>
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<tbody>
<tr>
<td><strong>A. General</strong></td>
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<tr>
<td>1.</td>
<td>Adopt or exclude model articles as appropriate.</td>
</tr>
<tr>
<td>2.</td>
<td>Can include provision for entrenchment.</td>
</tr>
<tr>
<td>3.</td>
<td>Existing companies only: remove or reflect provisions that are currently contained in the company's memorandum but will be regarded as provisions of its articles under the new law (e.g. objects clause).</td>
</tr>
<tr>
<td>4.</td>
<td>Can restrict the company's objects.</td>
</tr>
<tr>
<td><strong>B. Company Name</strong></td>
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<tr>
<td>1.</td>
<td>Private companies which are exempt from requirement for their names to conclude with “limited”: check that the articles comply with the Act.</td>
</tr>
<tr>
<td>2.</td>
<td>Can specify procedure for changing the company's name other than by special resolution.</td>
</tr>
<tr>
<td><strong>C. Members</strong></td>
<td></td>
</tr>
<tr>
<td>1.</td>
<td>Companies issuing share warrants: can provide that bearers of share warrants are deemed to be members either to the full extent or for any purpose defined in the articles.</td>
</tr>
<tr>
<td>2.</td>
<td>Companies issuing share warrants: can exclude bearer's entitlement to have, on surrendering his share warrant for cancellation, his name entered as a member in the register of members.</td>
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<tr>
<td>3.</td>
<td>Can make provision for the keeping of overseas branch registers.</td>
</tr>
<tr>
<td>4.</td>
<td>Can enable a member to nominate another person as entitled to enjoy or exercise all or any specified rights of the member.</td>
</tr>
<tr>
<td><strong>D. Directors</strong></td>
<td></td>
</tr>
<tr>
<td>1.</td>
<td>Can identify the purpose of the company, if this is other than the benefit of its members.</td>
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<tr>
<td>2.</td>
<td>Can authorise a director to act in a way which would otherwise infringe his duty to exercise independent judgment.</td>
</tr>
<tr>
<td>3.</td>
<td>Can remove provisions authorising what would in the past have been an infringement of a director’s duty to avoid a conflict of interest in relation to a transaction or arrangement with the company.</td>
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<tr>
<td>Public companies and private companies incorporated prior to 1 October 2008: can enable directors to authorise what would otherwise be an infringement of a director’s duty to avoid a conflict of interest.</td>
<td></td>
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<tr>
<td>Private companies incorporated on or after 1 October 2008: can remove the directors’ power to authorise what would otherwise be an infringement of a director’s duty to avoid a conflict of interest.</td>
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<tr>
<td>4.</td>
<td>Can require approval of the members to any transaction or arrangement which is authorised by directors under s175 or is disclosed to directors under s177.</td>
</tr>
<tr>
<td>5.</td>
<td>Can include provisions for dealing with directors’ conflicts of interest.</td>
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<tr>
<td>6.</td>
<td>Where a memorandum is required in relation to the approval by written resolution of a transaction with a director requiring members’ approval under the Act, can provide that an accidental failure to send or submit the memorandum shall be disregarded.</td>
</tr>
<tr>
<td>7.</td>
<td>Check that articles do not exempt a director from or provide for an indemnity (other than as permitted by the Act) against any liability in relation to the company.</td>
</tr>
<tr>
<td>8.</td>
<td>Can authorise directors to exercise the power to make provision for the benefit of employees in connection with the cessation or the transfer of business, except for the benefit of directors, former directors or shadow directors. Can impose additional requirements as to the exercise of this power.</td>
</tr>
</tbody>
</table>

**E. Company Secretary**

Private companies only: no longer required to have a secretary. s270

**F. Resolutions and Meetings**

1. Public companies only: no longer have power to pass written resolutions. s281(2)
2. Can require a higher majority than is required by the Act (or unanimity) for the passing of specified resolutions. s281(3)
3. Can provide for different voting rights than those set out in the Act subject to certain specific requirements. ss284-286
4. Private companies only: check that articles do not provide that a member has a different number of votes in relation to a resolution when it is passed as a written resolution and when it is passed on a poll. s285(3)
5. Can include provisions as to the making of objections to a person’s entitlement to vote and for the determination of any such objection to be final and conclusive. s287
6. Private companies only: ensure provisions relating to written resolutions are in accordance with the Act. ss288-300

Private companies only: can specify a percentage lower than 5% as the “requisite percentage” of members that can propose a written resolution.

Private companies only: can specify a different period of time for passing a written resolution to that set out in the Act.
7. Can include provisions in addition to those in the Act in relation to giving notice of meetings and resolutions and the conduct of a meeting.  

8. Minimum notice now reduced from 21 to 14 days for a special resolution or a resolution requiring special notice or (private companies only) of an annual general meeting.

   Can provide a longer notice period for calling a general meeting than that required by the Act.

   Private companies only: can specify a percentage higher than 90% but not more than 95% of the members to consent to short notice of a general meeting.

9. Can specify the persons to whom notice of general meetings must be sent.  

10. Can specify the content of notice of a general meeting.  

11. Can specify a manner, other than advertising in a newspaper, for giving special notice of a resolution.  

12. Can alter the provision that an accidental failure to give notice of a resolution or meeting is generally disregarded.  

13. Can specify a different quorum requirement to that set out in the Act.  

14. Can specify who may or may not be chairman of a general meeting.  

15. Check that articles do not exclude the right to demand a poll except in accordance with the Act.  

16. Private companies only: no longer required to hold annual general meetings.  

G. Proxies

1. Public companies only: a proxy now has the right to speak at a general meeting.  

2. Can provide more extensive rights to appoint more than one proxy.  

3. Check that articles do not require proxy appointments to be received earlier than as set out in the Act.  

4. Can require notice of termination of a proxy’s authority to be given to a person other than the company.

   Can require notice of termination of a proxy’s authority to be received earlier than the time set out in the Act but check do not exceed permitted times.

5. Can confer more extensive rights on members or proxies than are conferred by sections 324 to 330.
### H. Control of Political Donations and Expenditure

1. Can shorten the period for which a resolution authorising the making of political donations and incurring of political expenditure will have effect.  
   - s368(1)

2. Can restrict the directors’ power to shorten the period for which a resolution authorising the making of political donations and incurring of political expenditure will have effect.  
   - s368(2)

### I. Auditors

1. Private companies only: can require actual re-appointment of auditors to prevent their deemed re-appointment.  
   - s487(2)

2. Private companies only: can reduce the percentage of the members required to prevent the deemed re-appointment of an auditor.  
   - s488(2)

3. Check that articles do not contain provisions protecting auditors from liability other than as permitted by the Act.  
   - s532(3)

### J. Share Capital

1. Existing companies: can remove references to authorised share capital.  

2. Can provide for shares which do not normally carry voting rights at general meetings.  
   - s968(8)
   - s969(2)(b)
   - s972(4)(b)

3. Provide for the transfer of shares.  
   - s544

4. Can provide for share capital to be paid on a specified future date.  
   - s547(b)

5. Private companies with only one class of shares: can prohibit directors exercising power to allot shares etc.  
   - s550

6. Can authorise directors to allot shares etc up to a specified maximum and for up to five years.  
   - s551

7. Can authorise the company to pay commission for subscribing or procuring subscriptions for shares.  
   - s553(2)

8. Private companies only: can exclude existing shareholders’ pre-emption rights.  
   - s567(1)

9. Can confer a pre-emption right on shareholders corresponding to that contained in the Act.  
   - s568

10. Private companies with only one class of shares: can give directors power to disapply pre-emption rights.  
    - s569

11. Can give directors power to disapply pre-emption rights if they are generally authorised to allot shares under s551.  
    - s570

12. Can give directors power to disapply pre-emption rights in relation to a sale of treasury shares.  
    - s573
13. Can authorise the company to make provision for different amounts to be paid on shares. s581

14. Can include provisions for the forfeiture of shares or acceptance of shares surrendered in lieu. s617(5)(c) s659(2)(c) s662(1)(a) s668(1)(a)

15. No longer need authority in articles to sub-divide or to consolidate and divide shares. Can exclude or restrict the exercise of this power. s618(5)

16. Can prohibit or restrict the exercise of the power to redenominate share capital. s622(7)

17. Can make provision for the variation of class rights. s630(2)

18. No longer need authority in articles to reduce share capital. Can restrict or prohibit the reduction of share capital. s641(6)

**K. Acquisition of own Shares**

1. Private companies only: can exclude or restrict the power to issue redeemable shares. s684(2)

2. Public companies only: can authorise the issue of redeemable shares. s684(3)

3. Can authorise the directors to determine the terms, conditions and manner of redemption of redeemable shares. s685(1)

4. Can state the terms, conditions and manner of redemption of redeemable shares. s685(4)

5. No longer need authority in articles to purchase the company's own shares. Can restrict or prohibit the exercise of this power. s690(1)(b)

6. Private companies only: no longer need authority in articles to redeem or purchase own shares out of capital. Private companies only: can restrict or prohibit the exercise of this power. s709(1)

**L. Debentures**

1. Can provide for the closure of a register of debenture holders. s744(5)(a)

2. Can restrict the power to re-issue redeemed debentures. s752(1)(a)
<table>
<thead>
<tr>
<th>M.</th>
<th>Share Warrants</th>
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<tbody>
<tr>
<td>1.</td>
<td>Can authorise the issue of share warrants to bearer.</td>
<td>s779(1)</td>
</tr>
<tr>
<td>2.</td>
<td>Can authorise provision for the payment of future dividends on shares included in share warrants.</td>
<td>s779(3)</td>
</tr>
<tr>
<td>3.</td>
<td>Can disapply requirement to issue certificates in relation to shares included in a share warrant within two months of the surrender of the share warrant.</td>
<td>s780(2)</td>
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<tr>
<th>N.</th>
<th>Distributions</th>
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<tr>
<td>1.</td>
<td>Can prohibit the distribution of reserves in addition to the reserves which are made undistributable by the Act.</td>
<td>s831(4)</td>
</tr>
<tr>
<td>2.</td>
<td>Investment companies only: check that articles prohibit distribution of the company’s capital profits.</td>
<td>s833(2)(c)</td>
</tr>
<tr>
<td>3.</td>
<td>Can restrict on the sums out of which, or the cases in which, a distribution may be made.</td>
<td>s852</td>
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<tr>
<th>O.</th>
<th>Sending or Supplying Documents or Information</th>
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<tbody>
<tr>
<td>1.</td>
<td>Can include provisions requiring reasonable evidence of the authority of a person to send documents or information to the company on behalf of another person.</td>
<td>s1146(4)</td>
</tr>
<tr>
<td>2.</td>
<td>Can provide for deemed delivery times in relation to documents sent by the company to its members which differ from those prescribed in the Act.</td>
<td>s1147(6)(a)</td>
</tr>
<tr>
<td>3.</td>
<td>Check that the articles do not prevent the company communicating with shareholders by electronic means or by making documents available on a website, eg by referring only to hard copy delivery.</td>
<td>s1144(2), Schedule 5</td>
</tr>
<tr>
<td>4.</td>
<td>Can authorise the company to send documents to members by making them available on a website, so that the company can take advantage of the deemed consent provisions under paragraph 10.</td>
<td>Schedule 5, para. 10(2)(b)</td>
</tr>
<tr>
<td>5.</td>
<td>Can make provision relating to the supply of documents to joint holders of shares or debentures which differ from those set out in the Act.</td>
<td>Schedule 5, para. 16(4)</td>
</tr>
<tr>
<td>6.</td>
<td>Can make provisions relating to the supply of documents in the case of the death or bankruptcy of a shareholder which differ from those set out in the Act.</td>
<td>Schedule 5, para. 17(4)</td>
</tr>
</tbody>
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