Butterworths Corporate Law Update

BULLETIN EDITOR
Brenda Hannigan
Professor of Corporate Law, University of Southampton

Filing Instructions: Please file at the front of Binder 1.

RECENT DEVELOPMENTS

Financial Services Act 2012

The Financial Services Act 2012 comes into force on 1 April 2013 and it will be implemented through a rolling programme of commencement orders. It makes extensive amendments to the Financial Services and Markets Act 2000 and, in particular, provides for the replacement of the Financial Services Authority (FSA) by a Financial Policy Committee (FPC), a Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA). The functions of the UK Listing Authority (UKLA) will fall within the FCA.

Registration of company charges

New CA 2006, Part 25 provisions

Further to extensive consultations over the past three years, new provisions governing the registration of company charges will come into force on 6 April 2013: see the Companies Act 2006 (Amendment of Part 25) Regulations 2013, which insert new provisions into Part 25 into the CA 2006, replacing most of the 'old' Part 25.

The new scheme provides for the following.

- A single UK-wide scheme applicable to all companies incorporated under the CA 2006 or its predecessors; there will no longer be separate filing requirements for charges created by companies registered in Scotland.
- The requirement to register applies to every charge created by a UK-registered company over any of its property (wherever situated) subject to some exceptions. The old CA 2006, Part 25 listed the charges which needed to be registered, but in a significant simplification of the

legislation, the new Part 25 provides that all charges are registrable unless they fall within the exceptions in CA 2006, s 859A(6) (i.e. charges on cash deposits in favour of a landlord; charges created by a member of Lloyd's in connection with its underwriting business at Lloyd's; a charge excluded by or under any other Act).

- It will be possible for those presenting a charge for registration to do so electronically, but paper registration remains an option. A certified copy of the charge must be provided to Companies House for registration and this copy will be placed on the public record (certain personal and bank information and signatures can be removed). This means that only brief particulars of the charge will be required on registration (including whether there is a floating charge and whether there is a negative pledge) since any searcher of the public record can check for themselves what the charge actually states.
- The criminal sanction for failure to register a charge is removed (and with it the mandatory requirement for companies to register their charges), but as the sanction of invalidity where a charge is not registered within 21 days of its creation remains (CA 2006, s 859H), there still is a need to register the charge to avoid that sanction. In the event of non-registration, as before, the charge is void as against a liquidator, an administrator and any creditor of the company and the money secured by the charge becomes immediately payable: CA 2006, s 859H. Section 859E sets out, for the purposes of CA 2006, Part 25, a table identifying the date of creation of a charge – this is new.
- Although the Government did consider the inclusion of provisions governing constructive notice of charges, no such provision is included in the new CA 2006, Part 25.
- There is provision for amendments or additions to a charge to be notified to the registrar for registration where the new term prohibits or restricts the creation of any fixed security or any other charge having priority over, or ranking pari passu with, the charge; or the new term varies, or otherwise regulates the order of, the ranking of the charge in relation to any fixed security or any other charge (CA 2006, s 859O).
- Companies will no longer be required to maintain a register of charges, but they will have to keep for public inspection a copy of any charges created.

The new requirements for registration will apply to any charges created on or after 6 April 2013. The registration fee is £13 for paper registration and £10 for electronic filing.

The background to these changes can be found in various BIS consultation papers, see BIS Consultation Paper, *Revised Scheme for Registration of Charges created by Companies and Limited Liability Partnerships, Proposed revision of Part 25, Companies Act 2006* (August 2011), available at http://www.bis.gov.uk/assets/biscore/business-law/docs/r/11-1108-revised-scheme-registration-of-charges-part-25.pdf; and the initial consultation document, *Registration of charges created by companies and limited liability partnerships* (April 2010) available at http://www.bis.gov.uk/assets/biscore/business-law/docs/10-697-registration-of-charges-created-by-companies-proposals; together with the Government's response to that initial consultation at http://www.bis.gov.uk/assets/biscore/business-law/docs/g/10-1319-government-response-consultation-registration-of-charges.pdf.

Employee ownership and share buy backs

Government response – changes to CA 2006 in 2013

As noted in Update 155, the Department for Business, Innovation and Skills (BIS) has been consulting on modifications to CA 2006, Part 18, Chapter 4 governing share buy backs to give effect to the recommendations of the Nuttall Review of employee ownership which had concluded that the existing procedures are overly burdensome and something of a barrier and disincentive to direct employee ownership.

Following that consultation, the Government has now indicated that it intends to amend the CA 2006, by secondary legislation, to come into force during 2013.

The changes will:

- allow off-market share buy backs to be authorised by ordinary resolution (currently a special resolution is required: CA 2006, s 694) — this change is not limited to employee share schemes;
- allow for the prior approval of multiple off-market share buy backs for the purposes of or pursuant to an employee share scheme to be authorised by a single ordinary resolution (currently each contract needs to be authorised: CA 2006, s 694);
- allow private limited companies to pay for own shares in instalments where the buy back is for the purposes of or pursuant to an employees' share scheme (currently, the purchase price must be paid in full at the time of purchase: CA 2006, s 691). Instalment payments obviously pose some risk to the seller, but equally the seller must agree to instalment payments;
- allow for private limited companies to finance buy backs for the purposes of or pursuant to an employee share scheme out of capital subject to the signing of a solvency statement by the board of directors and shareholder approval by special resolution (in a manner similar to reduction of capital by way of a solvency statement, see CA 2006, s 642). The option remains for companies to use the extensive procedural protections which currently surround a purchase out of capital generally, see CA 2006, s 709 et seq;
- allow private limited companies, if permitted by their articles, to buy back shares using small amounts of cash (an amount not exceeding the

lower of £15,000 or the cash equivalent of 5% of share capital in any financial year) that does not have to be identified as distributable reserves;

- allow all companies limited by shares to hold their own shares in treasury and to deal with such shares as treasury shares (currently only traded companies can hold their shares as treasury shares: CA 2006, s 724) — this relaxation is not limited to shares acquired by way of an employee share scheme.

The Government's response, *Employee Ownership & Share Buy Backs, Implementation of Nuttall Review – Recommendation V: Government Response to Consultation* (February 2013, BIS/13/590) is available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/81699/bis-13-590-employee-ownership-and-share-buy-backs-implementation-of-nuttall-review-recommendation-v-government-response-to-consultation.pdf.

Financial Reporting Council

Reform of the Auditor's Report

The Financial Reporting Council (FRC) has issued a consultation paper proposing changes to the auditor's report (limited to UK premium listed companies) which in future would have to:

(a) describe the risks of material misstatement that were identified and assessed by the auditor and which had the greatest effect on the audit strategy;

(b) explain how the auditor applied the concept of materiality; and

(c) summarise the audit scope and in particular how the scope responded to the matters set out in (a) and (b).

The FRC notes that changes were made in 2012, primarily to the UK Corporate Governance Code, which require greater disclosure of information by auditors to the audit committee and greater disclosure by the audit committee of the work done by it and the information received by it from the auditors, all of which the FRC thought useful with regard to the outcome of an audit. But the FRC considers that investors would also find it useful to know about the inputs to the scope of the audit, such as the auditor's assessments of risk and materiality.

The FRC consultation document 'Revision to ISA (UK and Ireland) 700 (February 2013) is available at http://www.frc.org.uk/Our-Work/Publications/Audit-and-Assurance-Team/Consultation-Paper-Revision-to-ISA-(UK-and-Ireland.aspx. Comments are sought by 30 April 2013.

Going concern and reporting on risk – implementing the Sharman Report

Following the Sharman Report last year which examined how directors and auditors should address going concern and liquidity risk issues (see Update 153), the FRC is consulting also on the implementation of the Sharman recommendations via a new *FRC Guidance on Going Concern* to be issued later in 2013 coupled with amendments to the relevant Accounting Standards, all to be applied for financial years commencing on or after 1 October 2013.

See the Sharman Implementation Consultation Paper, available at http://www.frc.org.uk/Our-Work/Publications/Audit-and-Assurance-Team/Sharman-Implementation-Consultation-Paper.aspx.

The company law Red Tape Challenge — BIS

On 27 February 2013 Jo Swinson, Business Minister, announced the interim results for the company and commercial law theme of the Government's 'Red Tape Challenge'. The announcement also launched two consultations.

- *Company and business names*. This is a consultation on ways to improve the business and company names regulations, reducing their complexity and easing their burden on business. The consultation can be accessed at www.gov.uk/government/consultations/company-and-business-names-red-tape-challenge.

  Responses to the consultation are requested by **22 May 2013.**

- *Simpler business reporting for micro-entities*. The European Union has recently defined a new category of company, the 'micro-entity'. Micro-entities are very small limited liability companies and qualifying partnerships. This consultation sets out proposals for the UK implementation of the European Directive exempting micro-entities from certain financial reporting obligations. The government is seeking views on how best to implement the Micro Directive, which permits several exemptions.

  The consultation can be accessed at www.gov.uk/government/consultations/simpler-financial-reporting-for-micro-entities-the-uks-proposal-to-implement-the-micros-directive.

  Responses to the consultation are requested by **22 March 2013.**

Cross-border transfers of registered offices

EU consultation

The EU Commission has issued a consultation on the cross-border transfer of a company's registered office with a view to obtaining more in-depth information on the costs currently faced by companies when transferring their registered offices abroad and on the benefits that might arise from EU action on cross-border transfers. The Commission last addressed this issue in 2007 when it decided that the emerging caselaw from the Court of Justice facilitating freedom of establishment coupled with other options, such as using cross-border mergers (facilitated by the Cross-Border Merger Directive), or European Companies, SEs (facilitated by the European Company

Statute) meant that further intervention was unnecessary. The prime consideration now therefore is whether a direct mechanism for transfer of the registered office would be more cost-efficient and beneficial.

The consultation document is available at http://ec.europa.eu/internal_market/consultations/2013/seat-transfer/index_en.htm.

Statutory Instruments

SI 2013 No 395: the Late Payment of Commercial Debts Regulations 2013

These Regulations, which come into force on 16 March 2013, implement Directive 2011/7/EU on combating late payment in commercial transactions and do so by amending the Late Payment of Commercial Debts (Interest) Act 1998.

In particular, the regulations introduce a maximum payment period of up to 30 days where the purchaser is a public authority (the Government decided not to opt to extend that period to 60 days, as the Directive would have permitted), and in other cases a payment period of up to 60 days or longer as otherwise agreed. Where the payment period is longer than 60 days, the period must not be grossly unfair to the supplier.

The regulations also provide for a right to compensation for the reasonable costs incurred by a supplier in recovering a debt if those costs exceed the fixed sums of £40, £70 or £100 which already may be charged under the Act (depending on the size of the debt).

CASES

Piercing the corporate veil

Puppeteer not party to the puppet company's contracts

The Supreme Court has rejected an appeal in the *VTB Capital* case which primarily involved an issue as to permission to serve proceedings out of the jurisdiction, but also raised an issue regarding piercing the corporate veil. Dismissing the appeal, the Supreme Court divided 3–2 on the jurisdiction issue, but unanimously dismissed the appeal on the piercing ground.

The claimant company (VTB) had entered into a loan agreement providing $225m to a Russian company (RAP) which then defaulted on the loan. The claimants were pursuing claims in tort for deceit against RAP and its alleged controllers. Most of the case revolved around issues as to the appropriate forum for determining the tort claims. The piercing issue involved a plea by the claimant to be allowed to amend the particulars of claim to contend that the corporate veil of RAP should be pierced so as to render the alleged controllers of RAP parties to the loan agreement with VTB Capital and therefore jointly and severally liable for its breach.

The question for the court was whether there was a good arguable case for asserting contractual liability on that basis. At first instance and in the Court of Appeal, the court dismissed the suggestion that the veil piercing jurisdiction allows the court to find that those behind a company are parties to the contracts entered into by the company. The Supreme Court agreed unanimously that a contract claim based on piercing the corporate veil is unsustainable.

Interestingly, the respondents' case was not only that the controllers could not be made parties to the contracts of the company, but that there was no veil piercing jurisdiction in the first place.

Lord Neuberger noted that, while it was unnecessary to resolve that issue in this case, the attack on the existence of a piercing jurisdiction was worthy of serious consideration though Lord Wilson considered that counsel's submission that English law recognises no principle that the corporate veil may ever be lifted was 'a highly ambitious submission'. Lord Clarke noted that he would wish to reserve for future decision the question what is the true scope of the circumstances in which it is permissible to pierce the corporate veil. All their Lordships were agreed, however, that whatever the nature and extent of the piercing jurisdiction, there was an overwhelming case that it does not extend to making a person sheltering behind the veil liable as if he is a contracting party under a contract entered into by the company. Such an extension would be contrary to authority and principle: *VTB Capital plc v Nutritek International Corp* [2013] UKSC 5, [2013] All ER (D) 47 (Feb).

Breach of fiduciary duty

Personal or proprietary relief, again

A fiduciary (the respondent) received a €10m secret commission from the sellers of a hotel. He was the agent charged by the buyers (the claimants) with negotiating the price of the hotel. The buyers paid €211.5m for the hotel. At first instance, the court held that, in the light of the Court of Appeal ruling in *Sinclair Investments* (*UK*) *Ltd v Versailles Trade Finance Ltd* [2011] 2 BCLC 501, the appropriate remedy for the claimants was an account in equity in respect of the €10m and this was a personal and not a proprietary remedy.

On appeal, the only issue was whether the remedy was a personal or a proprietary remedy.

The Court of Appeal held that the proper characterisation of what occurred was that, by accepting the secret commission, the agent denied his clients the opportunity to acquire the hotel for €201.5m rather than €211.5m. He exploited the situation to obtain a personal benefit which he must be taken to hold on constructive trust for his principals and the claimants were entitled to a proprietary remedy.

The case is valuable for the extensive discussion by Lewison LJ and Sir Andrew Morritt of the implications and difficulties arising from the now controversial ruling in *Sinclair Investments*. There Neuberger LJ held (at [88]) that the fiduciary's obligation to account for any money or asset acquired in breach of his duties gives rise to a personal and not a proprietary claim 'unless the asset or money is or has been beneficially the property of the beneficiary or the trustee acquired the asset or money by taking advantage of an opportunity or right which was properly that of the beneficiary'. Only in these two categories is a proprietary claim appropriate. The decision in *Sinclair Investments* has been controversial with commentators divided on the merits of limiting proprietary relief in this way.

In the instant case, Lewison LJ pointed out that many relevant cases on these issues were not considered in *Sinclair Investments* and in particular the court did not consider *Bhullar v Bhullar* [2003] 2 BCLC 241. The Chancellor, Sir Andrew Morritt, noted that the expression 'properly that of the beneficiary' is not to be found in any reported cases and it is difficult to know the scope of this category identified by Lord Neuberger as giving rise to a proprietary claim. Pill LJ noted that, at bottom, this issue is a question of public policy and he saw force in the conclusion at first instance that the wrong here required only a personal remedy, though he ultimately agreed on proprietary relief.

The Chancellor ended his judgment by noting that the decision in *Sinclair Investments* has made the law more complex and uncertain, but whether that decision is right can only be resolved now by the Supreme Court. This very case showed, he said, the difficulty of drawing a borderline between personal and proprietary relief in the manner laid down by Lord Neuberger in *Sinclair Investments*. The Supreme Court will want therefore to address the policy issues here ranging from deterring fraud and corruption, to stripping fiduciaries of all benefits obtained, to the position of the fiduciary's creditors. The Supreme Court will also want to have an eye to the international perspective where the approach in *Sinclair Investments* is out of line with that in many other comparator jurisdictions such as Australia, New Zealand, Singapore and Canada: *FHR European Ventures LLP v Mankarious* [2013] EWCA Civ 17, [2013] All ER (D) 219 (Jan).

Re-registration from public company to private company

Application by objecting shareholders – definition of 'holder'

A public company passed the necessary special resolution to re-register as a private company (CA 2006, s 97(1)). Some minority shareholders objected and applied under CA 2006, s 98 as 'holders of not less in the aggregate than 5% in nominal value of the company's issued capital'.

The company successfully objected to their standing on the basis that the shares were registered in the name of a nominee shareholder and were not directly held by the minority beneficial interests who were objecting.

The court agreed that, on the wording of CA 2006, s 98(1), only the registered shareholder may object, not the indirect investors.

A further complication was that the registered holder, as a nominee for many investors, had voted some shares for the re-registration resolution as well as voting against the resolution. Section 98(1) rules out an objection 'by a person who has consented to or voted in favour of the resolution'.

The net result was that the indirect investors were not 'holders' entitled to object under CA 2006, s 98(1) and the registered holder, having voted some shares in favour of the resolution, could not object under s 98(1).

Norris J indicated some concern that this reading of the CA 2006, s 98(1) deprives indirect investors of the sort of protection which those who formulated the Companies Act 2006 thought 'ought to be extended to minority shareholders', but the wording of the section offered no other conclusion unless he was to embark upon what would be 'an impermissible form of judicial legislation'. The court gave judgment for the company: *Eckerle v Wickeder* [2013] EWHC 68 (Ch), [2013] All ER (D) 150 (Jan).

Removal of director

Relationship between shareholder agreement and articles of association

A shareholders' agreement provided for the appointment of J as a director of the company and his re-appointment at each subsequent AGM unless and until one of five 'termination events' occurred, such as a breach of fiduciary duty by J. The articles of association of the company contained a (common) provision that all the other directors acting together could give notice to a director to vacate office, whereupon the office is vacated. The directors (who included the parties to the shareholders' agreement) invoked that clause in the articles against J and notice was served on him to vacate office. Subsequently, at the next AGM, J was not re-appointed as a director.

J initiated proceedings seeking specific performance of the agreement and an order to the shareholder parties to the agreement to procure his appointment to the board. At first instance he succeeded on the basis of an implied term in the agreement that those party to the agreement would not join in a notice under the articles to remove him as a director (so such removal would not then be possible).

However, the Court of Appeal has (rightly) allowed an appeal.

McCombe LJ stressed in particular that where an agreement deals with the very subject matter at issue (the position of J on the board), there is little scope for going beyond it and adding/implying terms to what has been agreed. As the shareholders' agreement was silent about whether the shareholders as directors would not exercise their power of removal under the articles, the starting point was that the agreement had no effect on the power under the articles.

McCombe LJ noted that the agreement had been drawn up by lawyers with all parties being legally advised and it had been drawn up in the context of a dispute between the parties so, he said, in those circumstances it cannot be assumed that the express terms of the agreement did not represent the parties' true bargain. J was entitled to be appointed and re-appointed to the board so long as a termination event had not occurred. It would be, McCombe LJ said, 'a strong thing to import into the Agreement a further protection covering the same ground but going beyond that which is expressed'.

The absence of an implied term (preventing use of the power in the articles) did not render the agreement futile since J was still protected in his position as a director. The power in the articles to remove him by notice could only be exercised by all the other directors acting in good faith in the interests of the company and the support of any one other director would prevent the power being exercised against J. To imply the term, as had been done at first instance, would involve an impermissible re-writing of the parties' contract.

Laws and Lewison LJJ agreed. Lewison LJ thought there were two other significant considerations. First, he thought it was difficult to sustain an argument that terms are to be implied into an agreement made by contracting parties in one capacity (as shareholders) which results in a fetter on powers to act in another capacity (as directors), especially when shareholders may act in their own interests but directors can only exercise powers in the interests of the company. Furthermore, he thought that a putative director is entitled to take the articles at face value and to take up office on the footing that if the whole board votes to remove a director, that power will be an effective one: *Jackson v Dear* [2013] EWCA Civ 89, [2013] All ER (D) 275 (Feb).

Unfairly prejudicial petitions

Court rejects application for hearing in private

In a case concerning cross petitions under CA 2006, s 994 as to the unfairly prejudicial manner in which the affairs of a company were being allegedly conducted, the court was faced with an application by one side seeking orders that would result in certain disputed allegations of fact being dealt with by the court sitting in private, and orders that non-parties to the petitions, and in particular representatives of the media, should not be allowed to obtain copies of court documents in the case.

The application sought a private hearing saying that the allegations of misconduct were false, scandalous and put forward to pressure the applicants into a financial settlement contrary to their best interests and that publicity would threaten their health and personal safety and would harm relations between the UK and Saudi Arabia and the USA and Saudi Arabia. The applicants included members of the royal family of Saudi Arabia.

The court dismissed the applications. While the court could order a private hearing where that was necessary in the interests of justice, this case did not fall within that exception. Although the allegations against the applicants were very serious, it had not been clearly shown that those allegations would result in a serious interference with the private life of the applicants and whether such an interference would undermine their personal integrity. On the evidence, the applicants' assertions as to the harm that would follow from a public court hearing came nowhere near being clear and cogent evidence for the purpose of justifying a derogation from the principle of open justice. Having examined the various matters relied on, the importance of the open justice principle was greater than the importance to be attached to the reputations of the applicants.

It was not necessary in the interests of justice to conduct the relevant hearings in private. It followed that orders would not be made to prevent the media having access to documents that they needed to assist them in preparing a fair and accurate report of hearings that had, or ought to have, taken place in public. Given that the court hearings in the instant proceedings were to be carried out in public, there was no reason consistent with that conclusion that would persuade the court to withhold the documents sought by the media: *Re FI Call Ltd, Global Torch Ltd v Apex Global Management Ltd* [2013] EWHC 223 (Ch), [2013] All ER (D) 159 (Feb).

Multiple derivative claims permitted

Common law survives CA 2006, Part 11

An interesting issue concerning the scope of CA 2006, Part 11, Derivative Claims, has been resolved by Briggs J in favour of the retention of the prior common law on derivative claims other than with respect to what he described as the 'ordinary' derivative claim by a member of the allegedly wronged company. In the latter case, the matter is entirely governed by CA 2006, Part 11, but other derivative claims which were permitted at common law remain possible, he found.

The case concerned an application by A for permission to continue a derivative action concerning a claim for breach of fiduciary duty against the defendant director of company B where A was a member, not of company B, but of an LLP which held 100% of the shares in Company B. An 'ordinary' derivative claim could be brought by a member of Company B, but in this case the only member of Company B was the LLP which was under the control of the alleged wrongdoing director and therefore there was no member of Company B in a position to bring a derivative claim.

In those circumstances, Briggs J ruled that a member of a holding entity (whether a company or, as in this case, an LLP, made no difference, Briggs J said) could bring a derivative claim in respect of the wronged company, where the holding entity is itself in the same wrongdoer control as the wronged company.

Briggs J concluded that such a claim was possible at common law as a piece of procedural ingenuity designed to serve the interests of justice in appropriate cases. Typically, the derivative action at common law accommodated, as the legal representative of the company in wrongdoer control, a member of that company, but exceptionally it could be a member of its parent company where that parent company was in the same wrongdoer control.

The question for Briggs J then was whether that common law action had survived the enactment of CA 2006, Part 11, given that s 260(2) provides that a derivative claim may only be brought under Part II or in pursuance of a court order under s 994.

On that point, he concluded that 'applying the well established relevant principle of construction, Parliament did not expressly abolish the whole of the common law derivative action in relation to companies, even though by implication from the comprehensiveness of the statutory code it did do so in relation to derivative claims by members (as defined) of the wronged company'. Parliament chose to enact a comprehensive statutory code for the main version of a derivative claim, one brought by a member of the wronged company, but beyond that, the assertion that the remainder of the common law device was abolished failed because 'abolition was neither express nor a clear or necessary implication'.

A common law multiple derivative claim was possible then, though Briggs J did not seem to see much need for the 'multiple' tag, it is just a different type of derivative claim. On the facts, the court thought permission to continue the claim should be granted but subject to a relatively short stay for mediation to see if the parties could resolve their differences before the matter progressed to trial: *Re Fort Gilkicker Ltd, UPMS Ltd v Fort Gilkicker Ltd* [2013] EWHC 348 (Ch), [2013] All ER (D) 313 (Feb).

Correspondence about this bulletin may be sent to Stephen Barc, Technical Editor/Writer, Commercial & Property Law Team, LexisNexis, Halsbury House, 35 Chancery Lane, London WC2A 1EL (tel: +44 (0)20 7400 4674, email: stephen.barc@lexisnexis.co.uk). If you have any queries about the electronic version of this publication please contact the BOS and Folio helpline on tel: +44 (0)845 3050 500 (8:30am–6:30pm Monday to Friday) or for 24 hour assistance with content, functionality or technical issues please contact the Content Support Helpdesk tel: +44 (0)800 007777; email: contentsupport@lexisnexis.co.uk

Published by LexisNexis (www.lexisnexis.co.uk)

Printed in Great Britain by Hobbs the Printers Ltd, Totton, Hampshire

FSC www.fsc.org MIX Paper from responsible sources FSC® C020438

ISBN 978-1-4057-7440-6

9 781405 774406