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Butterworths Corporate Law Update

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RECENT DEVELOPMENTS

Small Business, Enterprise and Employment Bill

Companies House issues information on implementation

As a number of the measures in the SBEE Bill currently before Parliament affect filing requirements at Companies House in one way or another, Companies House has given some initial indication of how the implementation of the Bill will be rolled out. Overall, it is expected that implementation will take place over a period of 18 months from Royal Assent, which is expected to be March 2015, and will take place in three tranches, the key elements of which are noted below.

- **Tranche 1: Bearer shares –** 'bearer shares' will be abolished and any existing share warrants will need to be surrendered within nine months.
- **Tranche 2: Corporate directors –** The prohibition on appointing corporate directors will be introduced with some limited exceptions (see below). **Accelerated strike-off:** The time it takes to strike companies off the register will be reduced.
- **Tranche 3: Check and confirm –** This change will see the introduction of a requirement to 'check and confirm' company information on the register and notify changes, if necessary, at least once every 12 months. This 'check and confirm' process will replace the current obligation to file an annual return. **People with Significant Control (PSC) –** Companies will need to set up and maintain a register ('PSC register') identifying people with significant control over the company and this information will need to be filed at Companies House on incorporation and updated at 'check and confirm'. **Company registers** – private companies will be able to opt to keep certain information on the public register only, instead of statutory registers. This will apply to the registers of members, directors, secretaries, directors' residential addresses and the PSC register. **Directors' misconduct:** the disqualified

directors' regime will be updated and strengthened. **Statement of capital** – the requirements for the statement of capital will be simplified and applied consistently throughout the Companies Act 2006 (CA 2006).

The full text of the Companies House statement can be found at www.gov.uk/government/news/the-small-business-enterprise-and-employment-bill-is-coming.

Note that the Companies House website has moved and is now to be found at www.gov.uk/government/organisations/companies-house.

The latest version of the SBEE Bill, as amended by the House of Commons, is available at www.publications.parliament.uk/pa/bills/lbill/2014-2015/0057/lbill_2014-20150057_en_1.htm; with explanatory notes available at www.publications.parliament.uk/pa/bills/lbill/2014-2015/0057/en/15057en.htm.

BIS consults on Corporate Directors

Scope of exceptions to prohibition

One of the measures included in the Small Business, Enterprise and Employment Bill is a prohibition on the use of corporate directors, subject to certain exceptions which will be set out in accompanying regulations. The Department for Business, Innovation and Skills (BIS) is now consulting on the scope of those exceptions while noting that only 1.2% of the register, some 38,000, companies, currently use corporate directors.

BIS considers that:

- UK companies with shares admitted to trading on regulated markets (the main market of the London Stock Exchange) and UK companies with shares admitted to trading on prescribed markets in the UK (including the Alternative Investment Market, AIM) are cases for an exception given the degree of transparency which govern those markets.

This exception would be for the traded company and BIS is seeking views on how far the exception should extend within the group of which the traded company is a member, for example, whether it should be limited to wholly owned subsidiaries, or extend more broadly to subsidiaries controlled through voting rights or control of board appointments, or subsidiaries subject to some wider means of parental company influence.

BIS is also considering:

- Whether a subsidiary should be limited to appointing a parent company or another company in the group as a corporate director and whether the corporate director company should be required to have natural persons as its directors.

An exception would also apply for corporate directors of corporate trustees of pension funds, given the degree of sectoral regulation by the Pensions Regulator.

BIS considers that:

- The case for exceptions with regard to large public and private companies in group structures is more finely balanced. Any exception would be limited to large companies (i e one which does not meet the criteria to be a medium-sized company, as set out in CA 2006, ss 465–467) and the question to be considered is whether such companies have high corporate governance and transparency standards and a low risk of abuse which would warrant an exception.
- There may be a case for limited exceptions with regard to charitable companies and possibly for some Societas Europaea (SEs) (to ensure consistency with any exception available to public companies).

There is no proposal to change the position allowing corporate members of limited liability partnerships (LLPs), so they will be able to continue, though BIS welcomes further views on this matter and will look again at this issue in five years (sooner if evidence of abuse emerges) when the SBEE Act is reviewed. Likewise, there is no intention to change the use of authorised corporate directors by open ended investment companies (OEICs).

The intention is that the prohibitions and exceptions will apply to newly appointed corporate directors and to existing corporate directors after a transition period of one year. From the guidance given by Companies House as to implementation of the SBEE Bill, see above, it would seem likely that these provisions will come into force in April 2016 with a transition period through to April 2017.

See BIS, *CORPORATE DIRECTORS, Scope of exceptions to the prohibition of corporate directors*, (November 2014), BIS/14/1017. The closing date on this consultation is 8 January 2015. The full text of the consultation paper is available at www.gov.uk/government/uploads/system/uploads/attachment_data/file/378197/bis-14-1017-scope-of-exceptions-to-prohibition-of-corporate-directors.pdf.

BIS consults on Disclosure of Payments

Duty to report on Payment Practices and Policies

A further element of the SBEE Bill is additional reporting obligations requiring companies to report on payment practices and policies. BIS is consulting on the nature and extent of such new reporting obligations and notes that, as of July 2014, the overall level of late payment owed to small and medium-sized businesses was reported as standing at £39.4bn, with the average amount owed to a small business standing at £38,200.

The proposal is that:

- the new reporting requirements will apply to large companies, large limited liability partnerships, and all listed companies; and businesses will be required to report on an individual rather than on a group consolidated basis;
- companies will report on a series of proposed reporting metrics to give an indication of their payment performance: the proportion of invoices

paid beyond terms; the proportion of invoices paid over 30, 60 and 120 days; and the average time taken to pay invoices; and

- reporting will be on a standardised and mandatory basis, on a quarterly basis, and the information will be published on the company's website, where this exists, though BIS assume that most companies within these categories will have a website.

The aim is to allow suppliers to compare different customers against a standardised time frame of payment.

BIS is also considering whether firms should be required to provide additional information, in narrative form, to assist suppliers in understanding a firm's payment practices and performance.

- This additional information could include: a description of standard payment terms, (including changes that occurred over the reporting period and unilateral retrospective changes); a company's invoice dispute resolution process; e-invoicing; supply chain finance; and membership of voluntary payment codes.

Given recent public controversy over companies requiring payments from suppliers in order for the supplier to be on the company's list of preferred suppliers, BIS is also seeking views on whether these payments cause concern and, if so, what the role of the Government might be with regard to them.

See BIS, *Small Business, Enterprise and Employment Bill, Duty to report on Payment Practices and Policies* (November 2014), BIS 14/1203. The closing date for comments is 2 February 2015 and the consultation document is available at www.gov.uk/government/uploads/system/uploads/attachment_data/file/380183/bis-14-1203-duty-to-report-on-payment-practices-and-policies.pdf.

Statutory Instruments

SI 2014/3140 The Company, Limited Liability Partnership and Business Names (Sensitive Words and Expressions) Regulations 2014

One of the issues raised in the BIS Red Tape Challenge was whether there was scope to modernise and update the regulation of company names including the regulation of 'sensitive names' for which companies, limited liability partnerships and businesses need approval to use from Government Departments or other bodies. BIS found that seeking approval for a name can cause a delay in registration. Hence BIS has looked to reduce the list of sensitive names to allow a greater proportion of new companies to incorporate quickly.

This statutory instrument revokes the previous regulations of the same name, SI 2009/2615, and removes 26 'sensitive' names from the list, with effect from 31 January 2015.

Approval will no longer be needed, for example, for the use of 'national', 'European' or 'international' or 'United Kingdom'. Currently, anyone wishing to register a name including a 'national' word must demonstrate its' pre-eminence in the relevant activity across that nation while anyone using 'international' has to show trading overseas and confirm the country or countries involved.

It will no longer be necessary to have approval to use 'Group' or 'Holding' whereas previously Companies House required the company to be part of a group involving at least two or more existing companies and a holding company had to be such within the meaning of CA 2006, s 1159.

The full list of the 26 words for which approval is no longer needed can be found in the Annex to the Explanatory Memorandum to SI 2014/3140 which is available at www.legislation.gov.uk/uksi/2014/3140/pdfs/uksiem_20143140_en.pdf.

SI 2014/3209 Reports on Payments to Governments Regulations 2014

These regulations, which came into force on 1 December 2014, require large undertakings involved in extractive industries to report annually on payments made to Governments. The details were discussed in Corporate Law Update No 166.

New vehicle for employee shareholding

Government not to proceed

HM Treasury and HM Revenue and Customs consulted in 2014 on the introduction of a new vehicle to facilitate employee shareholding, but in the light of the responses to that consultation, the Government has announced that it has decided not to proceed.

Apart from technical issues with regards to the structure of any new vehicle and the safeguards which would be needed to prevent abuse, the consultation found there was no significant demand for a new vehicle from those most likely to use and benefit from it. Moreover, advisers were generally sceptical about whether the new vehicle would significantly reduce the need for specialist tax advice or necessarily increase employee share ownership.

The Government has said that it will continue to keep the individual issues raised by the discussion paper under review where it believes there may be scope to reduce burdens on those businesses wishing to use employee benefit trusts (EBTs) in a straightforward and simple manner.

The Government response is available at www.gov.uk/government/uploads/system/uploads/attachment_data/file/384227/ESV_summary_of_responses.pdf.

Review of sentencing for corporate manslaughter and health and safety offences

Sentencing to be linked to size of company

The Sentencing Council has issued a lengthy consultation document reviewing sentencing guidelines for health and safety and food offences and, given the close connection between corporate manslaughter and health and safety offences, in respect of corporate manslaughter also. The aim is to ensure a consistent approach across these offences, whether committed by individuals or organisations.

The Sentencing Council also considers that the principles of sentencing corporate offenders in health and safety and environmental offences laid down by the Court of Appeal in *R v Sellafield Ltd, R v Network Rail Infrastructure Ltd* [2014] EWCA Crim 49 should be highlighted in guidelines in this area.

In the light of criticism that fines imposed on organisations are too low relative to the harm caused, the culpability of the offender and, on occasions, to the means of the offender, the Council is proposing to introduce an approach to sentencing that more closely links the means of the offender – alongside the seriousness of the offence – to the final sentence.

In relation to organisations, the established principle which will be reflected in the guidelines is that the fine should be sufficiently substantial to have a real economic impact which will bring home to both management and shareholders the need to comply with legislation and achieve a safe environment for workers and members of the public.

For all the offences, the Council is proposing starting points that it considers to be reflective of the seriousness of the various offences and proportionate to the varying financial circumstances of the offender. Overall, the Council anticipates that the guidelines will mean that more serious offences committed by larger organisations will result in higher levels of fines.

For example, the starting point for a micro-organisation convicted of a serious offence under the Corporate Manslaughter and Corporate Homicide Act 2007 will be £450,000; for small organisations, £800,000; for medium organisations, £3m, and for large organisations, £7.5m.

There are four broad categories of organisation defined in the guidelines:

- Micro organisation: Turnover or equivalent: not more than £2 million.
- Small organisation: Turnover or equivalent: between £2 million and £10 million.
- Medium organisation: Turnover or equivalent: between £10 million and £50 million.
- Large organisation: Turnover or equivalent: £50 million and over.
- In addition, when sentencing 'very large' organisations – defined as those whose turnover very greatly exceeds the threshold for large organisations – it may be appropriate to move outside the range of sentence identified in the guideline to achieve a proportionate sentence.

The Sentencing Council consultation paper, Health and safety offences, corporate manslaughter and food safety and hygiene offences guidelines, (November 2014) is available at sentencingcouncil.judiciary.gov.uk/docs/

Health_and_safety_corporate_manslaughter_food_safety_and_hygiene_offfences_consultation_guideline_(web).pdf. The closing date for comments is 18 February 2015.

Cyber security

Guidance for non-executive directors

BIS has issued some useful guidance on cyber security for non-executive directors highlighting issues which they should consider and which they should raise with the board and audit committees in terms of assessing, managing and mitigating cyber risks to their businesses.

See HM Government, *Cyber Security: balancing risk and reward with confidence, Guidance for Non-Executive Directors,* (December 2014), BIS/14/1277, available at www.gov.uk/government/uploads/system/uploads/attachment_data/file/385009/bis-14-1277-cyber-security-balancing-risk-and-reward-with-confidence-guidance-for-non-executive-directors.pdf.

CASES

Equitable compensation

Supreme Court reviews link to loss

A bank lent £3.3m to a couple and released the money to the solicitor acting for the bank and the couple on the basis that a prior charge to Barclays would be redeemed in full and the bank would obtain a first charge over the couple's home for the £3.3m. In error, the solicitors redeemed only part of the debt owed to Barclays leaving Barclays with a prior charge for £273,777 with the bank having a second charge for its loan. The couple defaulted and the property was sold for £1.2m, of which the bank received £867,697.

The bank sued the solicitors and argued that they were entitled to compensation in the full amount of £3.3m on the basis that, when the solicitors failed to carry out their instructions, they acted in breach of trust and the bank was entitled to the reconstitution of the trust fund as it was at the time of the breach, ie £3.3m, which meant they were entitled to equitable compensation in that amount.

The Court of Appeal and first instance judge, though reaching the result by different routes, limited the compensation to £273,777 being the loss caused by the breach, applying *Target Holdings Ltd v Redferns* [1995] 3 All ER 785, a case which has been criticised for introducing a causation requirement in this context and for giving insufficient weight to the need for a trustee acting in breach of trust to reconstitute the trust fund.

This case gave the Supreme Court an opportunity to revisit *Target Holdings* and the broad principle identified there by Lord Browne-Wilkinson at [1995] 3 All ER 785 at 798, 'Equitable compensation for breach of trust is designed to achieve exactly what the word compensation suggests: to make good a loss in fact suffered by the beneficiaries and which, using hindsight and common sense, can be seen to have been caused by the breach'.

The Supreme Court has unanimously endorsed the approach in *Target Holdings* as correct with Lord Toulson noting that it would be 'a backward step' for the court to depart from it or re-interpret it. He also said that, absent fraud (which was not present in this case and which might give rise to other public policy considerations) it would not be right to impose or maintain a rule that gives redress to a beneficiary for loss that would have been suffered if the trustee had properly performed its duties.

Lord Reed pointed out that interpreting what Lord Browne-Wilkinson said as meaning that equitable compensation should be assessed in the same way as common law damages was to misunderstand what he had said. Lord Brown-Wilkinson did not intend to depart from the orthodox view that the equitable obligation is to restore the trust fund to the position it would have been in but for the breach and the measure of compensation should be assessed on that basis. The rest of the Supreme Court Justices agreed with Lords Toulson and Reed.

Essentially, a breach of trust entitles the beneficiary to a number of possible remedies, the normal one, in the case of misapplication of trust property, requires the trustee to restore the trust fund, either the assets or their monetary value, and questions of foreseeability or remoteness do not come into it. If the trust has come to an end (as was the case here), the trustee can be ordered to compensate the beneficiary directly. The purpose of the order is to place the beneficiary in the same position as he would have been in but for the breach. He is entitled to be compensated for any loss he would not have suffered but for the breach. In the case where the trustee has profited from his breach of trust, he is liable to account for the profit which ought properly to be held on behalf of the beneficiary.

The quantum of loss is to be fixed at the date of judgment as the figure then necessary to put the trust fund or the beneficiary back into the position it would have been in had there been no breach.

In this case, had the solicitors performed their trust, the bank would have had a first charge for £3.3m, as it was they had a second charge worth £273,777 less because of Barclay's prior interest. The measure of loss was £273,777. To hold otherwise would be to make the solicitors liable for the wholly inadequate security which the bank had accepted for the loan. As Lord Toulson noted, 'To say that there has been a loss to the trust fund in the present case of £2.5m by reason of the solicitors' conduct, when most of that sum would have been lost if the solicitors had applied the trust fund in the way that AIB had instructed them to do, is to adopt an artificial and unrealistic view of the facts.': *AIB Group* (*UK*) *plc v Mark Redler & Co Solicitors* [2014] UKSC 58, [2014] All ER (D) 49 (Nov).

Winding up petitions

Whether petition should be stayed given arbitration clause

The Court of Appeal has addressed the issue of whether and, if so, in what way, the stay provisions in the Arbitration Act 1996, s 9, apply to a petition (under Insolvency Act 1986 (IA 1986), s 122) to wind up a company on the ground of its inability to pay its debts where the debt on which the petition is based arises out of a contract containing provision for disputes to go to arbitration.

The appellants claimed in the region of £92,000, of which it was accepted that £64,000, roughly, was payable and a cheque for that amount was sent, but the rest of the claim was disputed with the result, in the view of the respondents, that the arbitration provision was triggered and hence the winding up petition should be stayed, applying Arbitration Act 1996, s 9. At first instance, the court did stay the petition on this basis.

The Court of Appeal dismissed the appeal but on a different basis. The court rejected the idea that Parliament, without any express provision to that effect, intended s 9 of the Arbitration Act 1996 to confer on a debtor the right to a non-discretionary order striking at the heart of the jurisdiction and discretionary power of the court to wind up companies in the public interest where companies are not able to pay their debts. A petition on the basis that the company is unable to pay its debts is not a claim for payment of a debt. Hence, the petition would not be stayed on the basis of the application of s 9.

However, IA 1986, s 122(1) confers on the court a discretionary power to wind up a company and it is entirely appropriate that the court should, save in wholly exceptional circumstances which are difficult to envisage, exercise its discretion consistently with the legislative policy embodied in the Arbitration Act 1996.

To do otherwise would encourage parties to an arbitration agreement, as a standard tactic, to by-pass the arbitration agreement and the 1996 Act by presenting a winding-up petition leaving the other party to the burden of satisfying the court that the debt was bona fide disputed on substantial grounds. That outcome would be entirely contrary to the parties' agreement as to the proper forum for the resolution of such an issue and to the legislative policy of the Arbitration Act 1996.

Hence, as a matter of the exercise of that discretion under IA 1986, s 122(1), the court could either dismiss or stay the petition so as to compel the parties to resolve their dispute over the debt by their chosen method of dispute resolution rather than require the court to investigate whether or not the debt is bona fide disputed on substantial grounds: *Salford Estates* (*No 2*) *Ltd v Altomart Ltd* [2014] EWCA Civ 1575, [2014] All ER (D) 102 (Dec).

Schemes of arrangement

Jurisdiction and class composition when dissenting creditor

In an important case which is to be reviewed by the Court of Appeal, the High Court was faced, unusually, with a contested application for sanction of a scheme of arrangement under CA 2006, Pt 26, involving a group of predominantly overseas companies but also two UK companies.

Hildyard J has provided a detailed lengthy judgment which explores the nature of the convening jurisdiction (convening by the court of meetings of members or creditors, as the case may be, to consider and approve a scheme under CA 2006, s 896) and the sanction hearing (when the court considers whether to sanction the scheme under CA 2006, s 899), both of which were contested by an opposing creditor.

The key points on the convening stage made by the court were:

(i) As regards the convening stage, the question is two fold, whether there is any real difference between the creditors in point of strict legal rights and if there is, by reference to the alternative if the scheme were to fail, whether objectively there is more to unite than divide the creditors in the proposed class, bearing in mind that the consequence of more classes may be to give some creditors a power of veto over a scheme.

(ii) Where insolvency is the correct comparator, then it is necessary to consider what would be the legal rights that the various creditors would have in an insolvency but for the schemes and the commercial value of those rights with and without the scheme as can best be estimated by reference to the likely outcome in a liquidation.

In the present case, the risk of imminent insolvency would have caused reasonable existing creditors to unite in a common cause. In all the circumstances, there was sufficiently more to unite than divide all creditors within a single class so as to make further classes unnecessary. In all the circumstances, there had not been sufficient reason demonstrated as to why the court should not accept the decisions of the meetings as representative, commercially sensible and fair.

The key points on the sanction stage were:

(i) As long established by the authorities, in the absence of some procedural or jurisdictional hurdle, or of some blot on the face of the scheme itself, the court should only decline to sanction a scheme if an intelligent and honest member of the relevant class acting in respect of his interest could not reasonably have approved it.

(ii) The proposition that the English court's jurisdiction did extend to the variation or release of claims against third parties designed to recover the same loss was entirely logical and necessary to protect schemes from being undermined by such collateral claims. But that proposition did not extend to the imposition of new obligations, even where the obligations could be said to be similar to existing ones arising in a tripartite context. The imposition of a new obligation to third parties was very different from the release in whole or in part of an obligation to such third parties. It was not necessary or wise for the court to express a final view in respect of the new obligations point (as this element of the scheme had been dropped once Hildyard J had made clear that he did not think he could approve a scheme which included it) save for acknowledging that the court felt especial unease in imposing new and more extensive obligations in the context of a cross-border scheme and on dissentients.

The jurisdiction of the court with respect to foreign companies.

All that had to be established to engage the jurisdiction of the court under CA 2006, Pt 26, was whether a company was 'liable' to be wound up under the IA 1986. In any cross-border context, it is important that the court should not trespass over the boundaries of comity by applying its jurisdiction in an exorbitant way.

Here there was a sufficient connection to warrant and justify the exercise of the court's jurisdiction under Pt 26. The parties had in accordance with their contractual agreements changed the governing choice of law to English law and the validity of that decision had not been questioned.

In all the circumstances, there was no real reason to doubt that the schemes would be recognised and enforced in the relevant EU jurisdictions and, accordingly, the court, in giving sanction, should not be acting in vain.

It followed that each of the schemes would be sanctioned: *Re Apcoa Parking Holdings Gmbh* [2014] EWHC 3849, 19 November 2014, [2014] All ER (D) 221 (Nov). An expedited appeal was heard on 9 and 10 December 2014 by the Court of Appeal whose ruling is awaited.

Service on overseas company

No link needed between proceedings and UK establishment

The claimant brought a claim against the defendant Korean company for damages for alleged repudiation of an option agreement regarding certain tanker contracts. The Korean company had registered an establishment (with an address in London) with Companies House, as required by CA 2006, s 1046. The claim was served at the establishment on a person who was registered at Companies House as authorised to accept service.

The defendant challenged the jurisdiction of the English court to hear the claim on the ground that service could only be effected at the company's establishment in the UK where the claim related to the establishment. The defendant also argued that proceedings should be stayed on the ground of forum non conveniens.

CA 2006, s 1139(2) provides: 'A document may be served on an overseas company whose particulars are registered under section 1046 – (a) by leaving it at, or sending it by post to, the registered address of any person resident in the United Kingdom who is authorised to accept service of documents on the company's behalf, or (b) if there is no such person, or if any such person refuses service or service cannot for any other reason be effected, by leaving it at or sending by post to any place of business of the company in the United Kingdom.'

The court, dismissing the defendant's application, ruled:

(i) The historical position has long been that in relation to service of overseas companies it was not necessary to establish any link between the subject matter of the proceedings and the business carried out in the UK. It followed that service on the authorised person at his registered address was good service under CA 2006, s 1139(2)(a).

(ii) Registering a UK establishment involved opening that establishment as a place of business in the UK. Once a place of business had been opened in that way then there was a place of business in the UK even if it had yet to start carrying on business. There was considerable force in the contention that the company should not be allowed to go behind the statement which it had made as a matter of public record that it had opened a UK establishment where it was carrying on business. The evidence established that the company was carrying out business activity and had a place of business at the material time. It followed that the London address was a 'place of business', at which the company had been validly served pursuant to CA 2006, s 1139(2)(b) and/or CPR 6.9(2) which also allows for service on an overseas company at any place of business of the company within the jurisdiction.

The court also rejected the application for a stay on the grounds of forum non conveniens for the evidence showed that England was clearly and distinctly the most appropriate forum for trial in the interests of the parties and for the ends of justice: *Teekay Tankers Ltd v STX Offshore & Shipping Co* [2014] EWHC 3612, [2014] All ER (D) 80 (Nov).

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