

Companies Act 2006 - simplifying the way in which businesses operate



One stated aim of the Companies Act 2006 (“the Act”) was to make it simpler for, in particular, small and medium sized companies to set up and operate. This note briefly considers how, by amending its Articles of Association, a company can benefit from some of the changes brought about by the Act.

Before the remaining provisions of the Act are implemented on 1 October 2009, companies should review their current constitutional documents in order to take advantage of these changes. Those involved in arrangements, such as shareholder and joint venture agreements, may also consider potential changes to those documents and their related Articles of Association. Those administering public companies will probably already be going through a more detailed review exercise in the light of the Act.

Articles of Association

Articles of Association are a public document open to inspection at Companies House and, together with the Memorandum of Association, form the constitutional documents of a company. Articles of Association may only be altered by special resolution by a company’s members.

Articles of Association are covered by part three of chapter two of the Act. Every company must have a set of Articles. These must be filed with Companies House, unless they are “model articles” which have not been modified. Model articles are essentially standard sets of Articles which have been prepared for the three most common types of companies:

- Private companies limited by shares;
- Private companies limited by guarantees; and
- Public companies.

Model articles for each type of company will apply by default to any company formed and registered under the Act. Companies can choose to include the provisions of model articles in their own Articles, with or without modification, provided of course they do not conflict with any mandatory provisions of the Act. For most small companies this is probably be the best way to proceed, i.e. adopting the provisions of model articles, perhaps in whole or possibly with one or two small modifications.

For all companies incorporated before 1 October 2009 no changes are required to their Articles of Association. However, an existing private company may wish to adopt the private company new model articles (with or without modifications), in place of its current Articles. These model articles were designed with the needs of small, owner managed businesses in mind and the provisions have been kept as simple as possible. The Department for Business, Innovation and Skills (DBIS), previously the Business, Enterprise and Regulatory Reform (BERR) and before that the Department of Trade and Industry (DTI), considers that any company needing more extensive Articles can adopt appropriate provisions from the model Articles for public companies.

Memorandum of Association

The company’s memorandum contains, among other things, the objects clause which sets out the scope of the activities a company is authorised to undertake. Historically this was drafted to give the company the widest possible powers. The changes under the Act which become effective on 1 October 2009, include:

- A significant reduction in the importance of a company’s memorandum. The Act provides that a memorandum for any new company will record only the names of the subscribers and the number of shares each subscriber has agreed to take in the company;
- The objects clause and all other provisions currently contained in the memorandum of an existing company will be deemed to be contained in its Articles of Association. However, the company will be able to remove some of these provisions by special resolution;

- A company's objects clause will be unrestricted unless its articles provide otherwise. This abolishes the need for companies to have objects clauses.

In summary, the Memorandum of Association for a new company will be of no relevance once that company has been formed. For existing companies, the Memorandum will to all intents and purposes disappear.

Entrenched Rights

The Act contains new rules dealing with the concept of entrenching certain rights in the Articles of Association. Absolute entrenchment will no longer be possible. Until now companies have been able to entrench certain elements of their constitution by putting them in their memorandum and providing that they could not be altered.

In future, some provisions of the Articles may be conditionally entrenched, so they can only be altered or appealed if certain procedures are complied with. These will be more restrictive than merely a special resolution. However, if all members choose they will be able to amend the articles. Companies will only be able to adopt entrenchment provisions on formation or if all shareholders agree.

New provisions ensure that the Registrar of Companies and any person searching the public register is notified that the Articles contain entrenchment provisions. The "existing companies' absolute entrenchment provisions" can remain as an unalterable for the remainder of the company's life, unless otherwise ordered by a court or other competent authority.

Examples of possible changes to the current Articles

As noted, a significant number of possible changes should be considered in respect of current Articles of Association, some of which are set out below:

1. Insert new wording to ensure directors' conflicts can be approved by the board in line with the Act
2. Remove the objects clause as is permitted under the Act, by passing a special resolution
3. Consider inserting updated wording on directors' indemnification
4. Consider new wording to cover written resolutions – a lower percentage of shareholders' votes is required under the Act than was previously required to pass written resolutions
5. Consider new wording to cover:
 - (a) new rules on calling meetings by short notice;
 - (b) the notice provisions for general meetings; and
 - (c) the threshold levels to pass resolutions.
6. The removal of the requirement for a private company to hold an annual general meeting might require changes to existing articles. It will also have an impact on the need to re-appoint auditors on an annual basis
7. Currently a company can only change its name by special resolution. Under the Act, if the Articles so provide, a name may be changed by a resolution of the directors
8. Consider new wording to amend various matters related to share capital. These might include: (a) the removal of the statement of authorised share capital (this will no longer be required); (b) power to increase authorised share capital which can be given to directors; and (c) power to cancel unissued shares
9. The government has suggested that statutory provisions should no longer be duplicated in a company's constitution.

There are other provisions which could benefit many companies. If you would like to discuss these or any of the issues raised here, please contact Nick Gould (nick.gould@incelaw.com) or James Gilbertson (james.gilbertson@incelaw.com).

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