

# Companies act 2006 essay

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The Companies Act 2006 which received Royal Assent in November 2006 consists of 1300 sections and is thought to be the single largest piece of legislation ever made.

This Act restates and replaces most of the company law provisions brought in by the previous Acts. The 2006 Act introduces an extensive range of changes to areas of company law such as the formation of a company, directors' duties and liabilities, members/shareholders rights and share capital maintenance. Although the majority of the provisions contained in the Act were not due to come into force until 1st October 2008, which has subsequently been postponed to 1st October 2009, a number of provisions such as the codification of directors duties, transactions with directors, written resolutions and changes to the law on meetings, electronic communications with members and increased rights for proxies came into force in 2007. The 2006 Act now enables companies to correspond with their members by electronic communication. Under the Companies Act 1985, companies were permitted to send notices of meetings and copies of their annual accounts and directors reports by means of electronic communication, provided that the company and the recipient agreed. The 2006 Act allows for members and companies to communicate via electronic means and the scope of the term has been widened. The company communications provisions of the Companies Act 2006 are to be found under sections 1143 to 1148 in Part 37 and the accompanying Schedules 4 and 5.

These provisions came into force in January 2007. The reasons for this part of the Act coming into force at this early stage was to insure the EU Transparency Obligations Directives were complied with and to allow early

delivery of the benefits of e-communications. These benefits include significant monetary savings to business, improved accessibility to information for all parties involved in the company, and provides a way for a direct dialogue between companies and shareholders. Members of a public company who hold at least 5% of the voting rights, or at least 100 members of a public company holding on average 1% of paid-up capital, can propose resolutions for an AGM agenda and to require the company to circulate details of the resolutions, which can be done in electronic form, to all members. Further, the members can require the company to circulate a statement up to 1000 words relating to a resolution or other matter which would be dealt with at an AGM. The 2006 Act also now enables indirect investors who are individuals who invest in units in a unit trust that invest in shares in the company to be more involved in, have a more direct relationship with their intermediary and be kept more informed of company decisions. Part 9, Section 145 of the 2006 Act, which came into force on 1st October 2007, gives rights to companies to allow them to empower a member to nominate other persons to enjoy his rights.

In order to empower their members with these rights, this provision will require to be detailed in the companies Articles of Association. If this is the case, the member may nominate several persons to apply his rights, so as to accommodate the splitting up of the exercise of the rights among numerous investors with beneficial interests in them. The Act recognises that in the a large number of cases the shares owned by beneficial owners in a companies are not the legal owners. The legal owners are usually institutional investors who the beneficial owners have channelled their investment. The Act

requires that companies allow the institutional investor to nominate the beneficial owner to have a right to all communications that would have been sent by the company to the legal owner. This applies in particular to the rights conferred by sections 291 and 293 (right to be sent proposed written resolution); (b) section 292 (right to require circulation of written resolution); (c) section 303 (right to require directors to call general meeting); (d) section 310 (right to notice of general meetings); (e) section 314 (right to require circulation of a statement); (f) section 324 (right to appoint proxy to act at meeting); (g) section 338 (right to require circulation of resolution for AGM of public company); and (h) section 423 (right to be sent a copy of annual accounts and reports)<sup>2</sup>. Unlike Section 145, the information rights provided for in Sections 146 to 151 apply to public companies whose shares are traded on an open market and are not subject to the provisions in the company Articles. The provisions laid down in Section 152 of the 2006 Act allows members who hold shares in a company on behalf of more than one person to vote and exercise his/her rights in different ways reflecting the wishes of different underlying holders.

This section also stipulates that a member does not require to exercise all his/her rights but does require to inform the company to what extent he/she is exercising the rights. If a member fails to inform the company of the way he/she is exercising his/her rights, the company can assume that he/she is exercising all his/her rights in the same way. <sup>3</sup> Section 153 sets down certain criteria that require to be met to allow indirect investors to join in certain member requisitions. This Section applies to Sections 314 (power to require circulation of statement); Section 338 (public companies: power to require

circulation of resolution for AGM); Section 342 (power to require independent report on poll); and section 527 (power to require website publication of audit concerns).

Apart from Section 145, rights in Part 9 are applied irrespective of and override the companies Articles of Association. However, a person who is bequeathed these rights by a member cannot commence an action against the company to enforce any rights delegated to him and these rights do not affect the requirements for an effective transfer or other disposition of the whole or part of a member's interest in the company<sup>5</sup> The Companies Act 2006 is also intended to promote the engagement of a long-term investment culture by heightening the power of proxies. The Companies Act 1985 specified that although members were entitled to appoint proxies, provisions on these appointments applied. Common law stated that members were entitled to appoint a proxy to attend a meeting on his/her behalf but that this entitlement was not an absolute right to allow the proxy to vote in his/her stead. <sup>6</sup> In terms of the Companies Act 1985<sup>7</sup>, all companies had to permit proxy voting at general and class meetings but limitations applied such as the proxies could not vote by a show of hands or speak at the meeting unless allowed for by companies Articles of Association or at the chairman of the meetings discretion. The proxies did have authority to demand or join in demanding a poll and could speak on behalf of the member at a general or class meeting. Although Table A, Article 59 allowed a member of a private company who held more than one share to appoint more than one proxy and for more than one proxy to attend company meetings, in terms of S372 of

the 1985 Act the member could not allow more than one proxy to attend on the same occasion.

Part 138 of the 2006 Act allows registered shareholders to appoint multiple proxies to attend, speak and vote at general meetings. This provision of the 2006 Act came into force on 1st October 2007. Under this provision a proxy attending a public company meeting will now have the right to speak and vote on a show of hands.

The member also has the right to appoint one proxy to each share held provided that each proxy is appointed to exercise the rights attached to a different share or shares held by the member. The rights of proxies may be extended by a company's Articles of Association, but not reduced unless expressly provided for. The effect on these changes is that proxies may significantly affect the conduct and voting at general meetings.

With the appointment of multiple proxies, each with a vote on a show of hands, poll voting may become more common. There are new requirements under the 2006 Act for quoted companies<sup>9</sup> if a poll is taken. These requirements are that quoted companies disclose on a website the results of any poll taken, if an independent report on a poll which has been taken or is still to be taken is requested by the members of a company, the directors must appoint an independent assessor within one week of the request for a report and a copy of the independent report on the poll must be placed on the quoted company's website. The Act also requires certain minimum information to be contained on the website. The 2006 Act also aims to increase the rights to members to sue directors for negligence and other

defaults and gives members rights to bring derivative claims on behalf of the company in certain circumstances.

These provisions are provided for in relation to Scottish companies under Part 1110, of the Act. A derivative claim is where an individual member takes action on behalf of the company against a director. An action against a director is usually brought on the instance of the companies board or the liquidator of a company. Prior to the 2006 Act a member could initiate proceedings against a director under common law. The rule in *Foss v Harbottle*<sup>11</sup> is about locus standi. In this case minority shareholders brought an action against directors in order to make them make amends to the company for their fraudulent acts. The court dismissed that action because the company in general meeting had refused to take any action against the directors. There are exceptions to this rule that have been recognised at common law.

One exception is that in cases where there has been an act which is illegal or ultra vires, individual shareholders may bring an action<sup>12</sup>; Another exception is that a shareholder is entitled to sue where a companies decision required more than a majority of shareholders agreement and was in fact implemented on a simple majority. A shareholder may also sue where there has been a denial of an individual membership right. <sup>13</sup> A derivative claim is where a shareholder takes action against the company on behalf of the company. The above exceptions are in respect of cases in relation to direct individual shareholder rights. Under the Act the cause of a derivative action must arise from the negligence, default, breach of duty or breach of trust by

a director and whether or not a director has benefited from the negligence or breach is not relevant<sup>14</sup>. Under the Act the Court has the power to prevent an action coming to trial if there is no prima facie case. The Court is to determine whether the claimant is acting in good faith by deciding whether or the action would have been brought by a person whose duty it was to promote the success of the company.

If the Court deems that the action should be dismissed an award of costs could be taken against the pursuer. Although it appears that the aim of the Companies Act 2006 is to relax the rules and regulations for forming and running a company, due to the fact that Act has only in part and only very recently come into force, a view of whether or not the statutory reform will benefit members is, in my view, not yet known. Whilst it appears that the changes made have been implemented to ensure each company runs in away to benefit its shareholders more than previously supplied for whether or not the Act will make a difference has yet to be established

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