

# Companies Act 2006 – part 2

## relevant to ACCA Qualification Paper F4 (ENG and SCT)

# articles of association

■ **This second article on the Companies Act 2006 (CA 2006) deals with the new provisions of the Act as they relate to articles of association.**

As was stated in the previous article – published in the February 2008 issue of *student accountant* – in future, a company's memorandum of association will be a very simple document of purely historic significance, providing evidence of the intention to form a company.

Section 17 of the CA 2006 specifically states that references in the Act to a company's constitution include the company's articles, resolutions, and agreements: it makes no mention of the memorandum of association. The articles of association are consequently to be recognised as the main element of a company's constitution and, in effect, they are the rules which govern a company's internal affairs and matters such as the allocation of powers between the members of a company and its directors. Companies are free to make such rules about their internal

affairs as they think appropriate, subject to the proviso that any such rules must not contain anything that is either contrary to the general law, or the specific provisions of the Act.

As before, the articles of association form a statutory contract between the company and its members, and between each of them (now s.33) and the previous common law will continue to be applied as appropriate.

Section 18 continues the requirement that all registered companies must have articles, and Section 19 gives the Secretary of State the power to prescribe 'default' model articles for the different types of company and these regulations will apply to companies where they have not registered any articles of their own, or have not specifically excluded the operation of the model article in question.

Under the previous legislation, the Secretary of State was only able to prescribe default model articles for companies limited by shares; under the new provisions, private companies limited by guarantee will have the option of not registering articles but relying

on the model articles for their regulation. As before, the articles must be contained in a single document and must be divided into consecutively numbered paragraphs (s.18(3)).

### ALTERATION OF ARTICLES

Section 21(1) restates previous provisions and permits a company to alter its articles by special resolution. The common law rules relating to such alterations still apply.

### ENTRENCHMENT OF ARTICLES

The previous legislation allowed companies to entrench certain elements of their constitution by putting them in their memoranda and stating that they could not be altered. Section 22 of the CA 2006 replaces that practice, but allows its effective continuation by permitting companies' articles to provide that certain provisions may be amended or repealed only if certain conditions are met, and that those conditions are more restrictive than would apply in the case of a special resolution.

Such a provision, referred to as a 'provision for entrenchment', may only be made in the company's articles on formation, or by an amendment of the company's articles agreed to by all members of the company. However, any such provision for entrenchment does not prevent alteration of the company's articles by agreement of all members of the company, or by order of a court or other authority which has power to alter the company's articles.

Nor, of course, does such a provision affect the power of a court to alter a company's articles. As a result of the above provisions, companies will not be permitted to state, in their articles, that an entrenched provision can never be repealed or amended.

Section 23 introduces a new requirement for a 'statement of compliance' – a notice of the existence of any entrenchment to be made known to the companies' registrar. Similarly, notice is also required if the company alters its articles to remove a provision for entrenchment, or if the articles are altered by order of a court or other authority to remove a provision for entrenchment or any other restriction on the power of the company to amend its articles.

The declared purpose of Sections 23 and 24 is to ensure that the registrar, and any person searching the public register, is made aware of the articles that contain entrenching provisions and that special rules therefore apply to the company's articles.

#### EFFECT OF ALTERATION OF ARTICLES ON A COMPANY'S MEMBERS

Section 25 restates Section 16 of the 1985 Act, which maintained the principle that members of a company are not bound by any alteration to the articles which require them to increase their liability to the company or to take more shares in the company. A member may, however, give written consent to such an alteration and will subsequently be bound by it.

If a company alters its articles, Section 26 states that a copy of the altered articles must be sent to the registrar not later than 15 days after the alteration takes effect. Should a company fail to comply with this requirement,

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the company (and every officer of the company who is in default) commits an offence. In addition, if the registrar becomes aware of a failure to comply with Section 26 then, under Section 27, the registrar may give notice to the company requiring it to rectify the breach within 28 days. If the company complies with the notice, it will avoid prosecution for its initial failure to comply. However, if the company does not comply, it will be liable to a civil penalty of £200, recoverable by the registrar as a debt, in addition to any criminal penalty that may be imposed.

#### EXISTING COMPANIES REGISTERED UNDER PREVIOUS LEGISLATION

Existing companies will continue to be subject to the version of the model articles in force when they were originally registered, although the current model articles have been changed to reflect the changed provisions on resolutions, meetings and electronic communications.

*The Companies (Tables A to F) (Amendment) Regulations 2007 (SI 2007 No 2541)* took effect from 1 October 2007, and it is possible that further revisions may have to be made in April 2008 when other parts of the CA 2006 come into effect. However, existing companies will be free to adopt, wholly or in part, the new model articles established under the CA 2006 once they are confirmed.

Finally, the memoranda of existing companies will contain constitutional information which will, in future, be set out in the articles. Section 28 provides that such material is to be treated, in the future, as part of the company's articles. Also, where the memorandum of an existing company contains a provision for entrenchment, then Section 28 states that the provision will be deemed to be in the company's articles.

#### DRAFT MODEL ARTICLES OF ASSOCIATION

Although the model articles have not as yet been introduced, the Government has issued *Draft Model Articles for Public Companies* for consultation purposes, and at [www.berr.gov.uk/files/file40794.doc](http://www.berr.gov.uk/files/file40794.doc) a draft of the expected regulations can be found.

The general structure of the regulations for public limited companies are set out below,

and the structure of the proposed regulations for other types of companies may be seen at the Department for Business Enterprise and Regulatory Reform website.

Part 1, Article 1, simply sets out the definitions and interpretation to be applied in the articles. Part 2 deals with directors. Articles 2–5 specifically deal with directors' powers and responsibilities:

- 2 Directors' general authority
- 3 Members' reserve power
- 4 Directors may delegate
- 5 Committees.

Articles 6–18 relate to decision making by directors:

- 6 Directors to take decisions collectively
- 7 Calling a directors' meeting
- 8 Participation in directors' meetings
- 9 Quorum for directors' meetings
- 10 Meetings where total number of directors is less than quorum
- 11 Chairing of directors' meetings
- 12 Voting at directors' meetings: general rules
- 13 Chairman's casting vote at directors' meetings
- 14 Alternates voting at directors' meetings
- 15 Conflicts of interest
- 16 Proposing directors' written resolutions
- 17 Adoption of directors' written resolutions
- 18 Directors' discretion to make further rules.

Sections 19–23 deal with the appointment of directors:

- 19 Methods of appointing directors
- 20 Retirement of directors by rotation
- 21 Termination of a director's appointment
- 22 Directors' remuneration
- 23 Directors' expenses.

Articles 24–26 deal with alternate directors:

- 24 Appointment and removal of alternates
- 25 Rights and responsibilities of alternate directors
- 26 Termination of an alternate directorship.

Part 3 relates to decision making by members. Articles 27–32 deal with the organisation of general meetings:

- 27 Members can call a general meeting if not enough directors

- 28 Attendance and speaking at general meetings
- 29 Quorum for general meetings
- 30 Chairing of general meetings
- 31 Attendance and speaking by directors and non-members
- 32 Adjournment.

Articles 33–40 deal with voting at general meetings:

- 33 Voting: general
- 34 Errors and disputes
- 35 Demanding a poll
- 36 Procedure on a poll
- 37 Content of proxy notices
- 38 Delivery of proxy notices
- 39 Amendments to resolutions
- 40 No voting of shares on which money owed to company
- 41 Class meetings.

Part 4 deals with shares and distributions.

Articles 42–44 deal with the issue of shares:

- 42 Powers to issue different classes of share
- 43 Payment of commissions on subscription for shares
- 44 Company not bound by less than absolute interests.

Articles 45–48 deal with share certificates:

- 45 Certificates to be issued except in certain cases
- 46 Contents and execution of share certificates
- 47 Consolidated share certificates
- 48 Replacement share certificates.

Articles 49 and 50 deal with shares not held in certificated form:

- 49 Uncertificated shares
- 50 Share warrants.

Articles 51–61 deal with partly paid shares:

- 51 Company's lien over partly paid shares
- 52 Enforcement of the company's lien
- 53 Call notices
- 54 Liability to pay calls
- 55 When call notices need not be issued
- 56 Failure to comply with call notices: automatic consequences
- 57 Notice of intended forfeiture
- 58 Directors' power to forfeit shares

- 59 Effect of forfeiture
- 60 Procedure following forfeiture
- 61 Surrender of shares.

Articles 62–68 deal with the transfer and transmission of shares:

- 62 Transfer of certificated shares
- 63 Transfer of uncertificated shares
- 64 Transmission of shares
- 65 Transmittees' rights
- 66 Exercise of transmittees' rights
- 67 Transmittees bound by prior notices
- 68 Procedure for disposing of fractions of shares.

Articles 69–76 deal with distributions:

- 69 Procedure for declaring dividends
- 70 Calculation of dividends
- 71 Payment of dividends and other distributions
- 72 Deductions from distributions in respect of sums owed to the company
- 73 No interest on distributions
- 74 Unclaimed distributions
- 75 Non-cash distributions
- 76 Waiver of distributions.

Article 77 deals with the authority to capitalise and appropriation of capitalised sums.

Part 5 deals with miscellaneous provisions.

Articles 78–80 deal with communications:

- 78 Means of communication to be used
- 79 Addresses and other contact details
- 80 Failure to notify contact details.

Articles 81–84 deal with administrative arrangements:

- 81 Company seals
- 82 Destruction of documents
- 83 No right to inspect accounts and other records
- 84 Provision for employees on cessation of business.

Articles 85 and 86 deal with directors' indemnity and insurance:

- 85 Indemnity
- 86 Insurance. ■

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