

Company Law Reform

MODERN COMPANY LAW

For a Competitive Economy

The Strategic Framework

A Consultation Document from
The Company Law Review Steering Group

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February 1999

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Introductory

1. This Consultation Document is the first to be issued by the Steering Group set up to take forward a fundamental review of company law. It:

- describes the work of the Review so far and the proposed arrangements for taking it forward;
- analyses a number of key substantive issues for the purpose of consultation, and indicates a preferred way forward in some cases; and
- examines issues relating to the legislative form of implementation and the institutional structures for ongoing reform.

The terms of reference suggested in March 1998 have not been changed: the focus of the Review remains core company law, although the need to deal with relationships between such law and wider areas is recognised.

Overall Approach (Chapter 2)

2. The objective is modern law supporting a competitive economy, in a coherent and accessible form, providing maximum freedom for participants to perform their proper functions, but recognising the case for high standards and for ensuring appropriate protection for all interested parties. Account needs to be taken of current change, particularly globalisation, the impact of the EU's company law harmonisation programme, modern patterns of regulation and ownership, changing asset structures and the importance of small and closely held businesses.

In principle there should be presumptions:

- against interventionist legislation and in favour of facilitating markets, including provision for transparency of information, wherever possible;
- in favour of minimising complexity and maximising accessibility of the rules—complexity should only arise where the substance demands it and the law should be structured on 'think small first' principles;

- against creating criminal offences unless the subject matter demands it; and
- in favour of allocating jurisdiction to the most suitable regulatory bodies, avoiding duplication and conflict.

3. On this basis the Review has addressed seven key areas through working groups and made an initial analysis of accounting and reporting issues, recognising that empirical work would be required once policy issues came into focus.

European and Comparative Material

4. Chapter 3 sets out the European Union and Human Rights context. Chapter 4 briefly reviews relevant trends in key foreign jurisdictions.

Eight Key Areas, and Accounting and Reporting Issues

5. Chapter 5.1 analyses the interests which company law should serve, focusing on the actual changes to the law which different approaches would imply. A case is recognised for ensuring that company managers have regard, where appropriate, to the need to ensure productive relationships with a range of interested parties and have regard to the longer term. A distinction is drawn between the ‘enlightened shareholder value’ approach, which asserts that this can be achieved within present principles, but ensuring that directors pursue shareholders’ interests in an enlightened and inclusive way, and the ‘pluralist’ approach, which asserts that co-operative and productive relationships will only be optimised where directors are permitted (or required) to balance shareholders’ interests with those of others committed to the company.

6. It is acknowledged that current law is not widely recognised as embracing the enlightened shareholder value approach. Options for change are assessed. The pluralist approach and its implications for legal discretions, duties, remedies and board structures are examined. The importance of transparency in achieving satisfaction of a wider range of interests, and the case for enabling, or requiring, directors to satisfy wider social or philanthropic objectives, are considered.

7. Chapter 5.2 addresses the needs of small and closely-held companies, which are not well served by the present Act, either in substance or form. The merits of new free-standing legislation for such companies, as opposed to an integrated rewrite of existing law, are examined. A provisional conclusion is expressed for the latter, rewriting the legislation on a ‘Think small first’ basis, with appropriate flexibility to suit the needs of such companies, while retaining integrated legislation which provides for all.

8. Chapter 5.3 and 5.4 make proposals for simplifying the law relating to company formation and maintenance of share capital. These include:

- the clarification and reform of the rules relating to capacity of companies and their agents and validity of transactions with third parties;
- removing the need for court approval of capital reductions;
- a simplified financial assistance regime, dependent on member approval and solvency certification; and
- introduction of no par value shares.

European Directive constraints on these proposals (particularly for public companies) are recognised, but the case is made for negotiating their reform.

9. Chapter 5.5 maps present boundaries between various regulatory and enforcement jurisdictions and raises issues of principle.

10. Chapter 5.6 assesses the current international attractiveness of our law, examines rules on international jurisdiction and application of British law and considers possible changes. It also assesses the regime for foreign companies established here.

11. Chapter 5.7 explains the relevant information and communications technologies and assesses the case for changing the law in particular instances. Proposals are made on company meetings, communications with members and the holding of company information. A broad power to amend the Act to respond to change is also proposed.

12. Chapter 6 describes key issues in the field of financial and other reporting. These include the form and content of accounts; the role of accounting standards and international standards; exemptions for small and medium sized companies; the directors' report and the case for its expansion to achieve wider accountability; the role and responsibilities of auditors; the growth in non-statutory reporting; and electronic communications. It seeks initial views, on these issues and more widely, to assist the approach to this work in the next phase.

Other topics addressed in the Document

13. Chapter 7 describes related work being undertaken by the English and Scottish Law Commissions.

14. Chapter 8 discusses options for the form of new legislation to implement our proposals, and the related question of ongoing institutional mechanisms for reform.

15. Chapter 9 describes the priorities and method for carrying work forward to the next stage, through seven further working groups¹ and empirical research projects. Further consultation on this work is expected at the end of 1999, with final consultation on the overall outcome in late 2000.

16. Since this is a high level document, there will be further consultation on all the ground covered in it, and all that yet to be covered. This will be at a more detailed level where the work has progressed already to initial preferences (i.e. chapters 5.3, 5.4, 5.6 and 5.7) but in other key areas will be in two stages, at a high level and then again in detail.

17. Chapter 10 restates the questions for consultation.

¹: Focused on:- the range of vehicles for company organisation (including developing the proposals on the small and closed company and the shape of the legislation); governance (i.e. the rules governing the structure and internal relationships of the various components of a company) (two groups); accounting, reporting and disclosure; further work on the priority issues covered in Chapter 5; a number of more specific subjects (such as groups and solvent mergers and dissolutions); and finally overlap and transitional questions.