



t. 0845 225 2845 f. 0870 432 0247 e. info@holdenassociates.co.uk

The Companies Act 2006 – Client Briefing No. 2

The Companies Act 2006

Introduction

As our corporate clients will be aware, the Companies Act 2006 (the Act) is being introduced over a period of time by statutory instrument, with the Government having set a target date of October 2008 to have the complete Act in force.

Certain parts of the Act came into force on 8 November 2006 (the day on which the Companies Bill received Royal Assent) with additional provisions coming into force on 1 January and 20 January this year.

Still more provisions came into force on 6 April and we set out details of these provisions below. Should you require further information, please do not hesitate to contact us.

Provisions coming into force on 6 April 2007

The provisions of the Act which came into force on 6 April 2007 are set out in Statutory Instrument 2006 No. 3428 (C.132) *“The Companies Act 2006 (Commencement No.1, Transitional Provisions and Savings) Order 2006”*.

Advice: You can download a copy of the Statutory Instrument, free of charge, by going to the Office of Public Information website at:
http://www.opsi.gov.uk/si/si2006/uksi_20063428_en.pdf.

In addition, you can download the Explanatory Memorandum at:
http://www.opsi.gov.uk/si/em2006/uksiem_20063428_en.pdf

We summarise the new provisions below:

Section 1063 (fees payable to registrar), so far as not in force by virtue of article 3(3)

This section gives the Secretary of State the power to set fees by regulations in relation to any function of the registrar of companies and in relation to the provision of services and facilities incidental to his functions. It replaces section 708 of the 1985 Companies Act (the 1985 Act), but is more specific about the types of services for which fees may be charged, although the list is not exhaustive.

As now, fees relating to the normal statutory filing obligations of companies under companies legislation will be set by regulations made by the Secretary of State. It will also be possible for fees to be charged for any ad hoc and bespoke discretionary services which Companies House wishes to provide.

The 1985 Act (section 708(5)) provides that the registrar can himself determine fees for services for which there is no direct legal obligation. Subsection (5) of section 1063 replaces this with a more general power for the registrar to determine fees where no fee has been set in regulations by the Secretary of State. Such fees might relate, for example, to the introduction of new services (eg those made possible by new technologies) which could not have been anticipated when the Secretary of State last made fees regulations; or for services such as seminars and road shows which Companies House arranges.

Advice: You can find details of fees currently being charged by the registrar on the Companies House website at: <http://www.companieshouse.gov.uk>.

Section 1176 (power of Secretary of State to bring civil proceedings on company's behalf)
This section repeals section 438 of the 1985 Act and amends sections 439 and 453 of that Act. Section 438 of the 1985 Act gave the Secretary of State the power to bring civil proceedings on a company's behalf. Section 439 concerns the expenses of investigating a company's affairs and section 453 relates to the investigation of overseas companies.

Advice: This section is of a specialised nature and relates to company investigations.

Section 1177 (repeal of certain provisions about company directors)

This section repeals a number of provisions in the 1985 Act concerning directors. The following sections are repealed:

- Section 311 – Prohibition on tax-free payments to directors.
This section prohibited a company from paying a director remuneration free of income tax. The Law Commissions recommended its repeal in their 1998 report, *Company Directors: Regulating Conflicts of Interest and Formulating a Statement of Duties*, on the grounds that the tax which the company agreed to pay is itself taxed as part of the emoluments of a director and that the company is required to disclose in its annual accounts an estimate of the tax which it has undertaken to pay.
- Sections 323 and 327 – Prohibition on directors dealing in share options.
Section 323 of the 1985 Act prohibited directors (including shadow directors) from buying “put” and “call” options in listed shares or debentures in the company or another in the same group. This prohibition is extended to spouses and minor children of directors by section 327 of the 1985 Act. The repeal of these sections was recommended by the Law Commissions in their 1998 report, *Company Directors: Regulating Conflicts of Interest and Formulating a Statement of Duties*.
- Sections 324 to 326 and 328 to 329, and Parts 2 to 4 of Schedule 13 – Register of directors' interests (see advice box below)
- Sections 343 and 344 – Special procedure for disclosure by banks.
These sections made special provision for banking companies and the holding companies of credit institutions, allowing them to disclose in their annual accounts abbreviated particulars of loans, quasi-loans and credit transactions with directors or their connected persons. Section 413 of the 2006 Act, which replaces the annual accounts disclosure requirements of the 1985 Act in respect of loans, quasi-loans and credit transactions, makes its own special provision for banking companies and the holding companies of credit institutions. Sections 343 and 344 of the 1985 Act are therefore no longer needed.

Advice: The main repeal of practical significance concerns the register of directors' interests. The 1985 Act required a director to notify his company if he or certain close relatives acquired shares in the company. In addition, the company had to enter details of such shareholdings in its register of directors' interests.

The repeal of these sections will mean that a director will no longer have to notify the company of such shareholdings and the company need no longer maintain a register of directors' interests.

Note that in view of this repeal, Companies House will no longer accept Form 325 (Location of register of director's interests in shares), or Form 325a (Notice for inspection of a register of directors interests in shares kept in a non-legible format).

Note also that directors will not be required to disclose their interests in shares in the directors' report in the annual accounts for reports signed after 6 April 2007.

Section 1178 (repeal of requirement that certain companies publish periodical statement)

This section repeals section 720 and Schedule 23 of the Companies Act 1985 which required certain types of company (eg insurance companies) to publish periodic statements in a defined format. This disclosure requirement has been superseded by specialised regulatory developments in particular fields of financial services.

Advice: Unless your company is subject to specialised regulations, you can safely ignore this topic.

Section 1179 (repeal of requirement that Secretary of State prepare annual report)

This section repeals section 729 of the 1985 Act which means that there will no longer be a statutory annual report by the Secretary of State to Parliament, but note that the DTI will continue to produce the information.

Section 1281 (disclosure of information under the Enterprise Act 2002)

This section amends Part 9 of the Enterprise Act 2002 to enable public authorities, in certain circumstances, to disclose information where the information is to be used in civil proceedings or otherwise for the purpose of establishing, enforcing or defending legal rights.

Advice: A specialised area that can safely be ignored by most companies.

Repeal of section 41 of the 1985 Act (authentication of documents on behalf of company)

This section imposed a requirement to have a document or proceeding requiring authentication by a company to be authenticated by the signature of a director, secretary or other authorised officer. This is now no longer needed as this requirement has been overtaken by common law developments and scope to use a company's own articles to provide for this.

Repeal of sections 293 and 294 of the 1985 Act (age limits for directors)

This repeal means that a director of a public company or a private company that is a subsidiary of a public company will no longer be prohibited from being a director of the company when he has attained the age of 70.

Advice: This repeal only affects public companies or subsidiaries of public companies that have such directors.

The following provisions of the Companies Act 2006 came into force on 6 April 2007 so far as is necessary for the purposes of the provisions set out above.

- Section 1060 which states that there shall continue to be a registrar of companies who shall be appointed by the Secretary of State.
- Section 1061 which states that the registrar shall continue to carry out those functions conferred by the Companies Acts and other specified enactments.
- Section 1284 which extends the Companies Act 2006 to Northern Ireland.

The accounting requirements of the Companies Act 2006

Introduction

The provisions in the Act that relate to the statutory accounts of a company will be of special interest to all companies. We set out below a summary of the main provisions relating to accounts which are contained in the Act, with special emphasis on any new provisions or provisions that have or will amend provisions included in previous legislation.

The following general points should be noted:

Commencement dates

The Part of the Act that contains the provisions relating to the accounts and reports of companies will, in the main, come into effect from 6 April 2008. However, the following provisions (details of which are set out below) come into force on the following dates:

20 January 2007

Section 463 which sets out a statutory basis of directors' liability to the company in relation to the Directors' Report (including the Business Review) and the Directors' Remuneration Report.

1 October 2007

Section 417 which contains provisions relating to the content of the business review contained in the directors' report.

Form and content of accounts

Section 396 of the Act states that a company's individual accounts "must comply with provision made by the Secretary of State by regulations ..."

As at the date of this publication no such regulations have been made but it is unlikely that there will be any material changes to the format and content of accounts from that which exist at present.

Accounts and Reports

The main provisions in the Act that relate to accounts and reports will be found in Part 15 of the Act. Those provisions that relate to the audit of accounts will be found in Part 16, Chapter 1.

Chapter 1 of Part 15 of the Act commences with setting out the "scheme" of this Part of the Act.

Section 380 states that the requirements of this Part of the Act relate to each financial year of a company and that the provisions of the Act in relation to accounts and reports will differ according to the type of company involved. The main differences will be because a company is a small company or an unquoted company.

This section also makes the important point that the various provisions are set out in a particular order, as follows:

- Small company provisions are set out before those provisions applying to other companies;
- Provisions applying to private companies are set out before those provisions applying to public companies; and
- Those provisions applying to unquoted companies are set out before those provisions applying to quoted companies.

This order of layout emphasises one of the key principles of the Act – "Think small first".

Chapter 1 continues by setting out what constitutes a small company and distinguishes between the qualification requirements for small companies in general and companies that are parent companies. There have been no material changes to the qualification criteria set out in the 1985 Act and these are still based on turnover, balance sheet total and number of employees. The various qualification thresholds are set out in sections 382 and 383 and these are identical to those in the 1985 Act.

However, section 392 now clarifies the term “balance sheet total” as no definition was contained in the 1985 Act. Balance sheet total is defined as “the aggregate amount shown as assets in the company’s balance sheet”.

Section 384 lists those companies that are excluded from the small company regime and this list is much the same as under the 1985 Act, although certain specialised companies are now included, eg an e-money issuer.

Section 385 defines quoted and unquoted companies and states that the Secretary of State may amend the definition of such companies by regulations.

Section 386 of the Act imposes a duty on a company to keep accounting records. Under the 1985 Act a company had to keep “proper” accounting records. Under the 2006 Act a company must keep “adequate” accounting records.

Advice: The use of the word “adequate” instead of “proper” should cause no difference in approach by companies, but you should have regard to any statements or other documents that at present refer to the word “proper”.

What constitutes adequate accounting records is the same as under the 1985 Act.

Sections 387 to 389 deal with the offence of failure to keep adequate accounting records, where the records must be kept and the period of time they must be kept. The provisions are much the same as those contained in the 1985 Act.

Sections 389 to 392 set out the provisions relating to a company’s financial year, its accounting reference period and accounting reference date. There are no material changes in relation to these provisions.

Chapter 4 of Part 15 of the Act (sections 393 to 414) contains provisions relating to the preparation of accounts that give a true and fair view and the documents which must be included in accounts, eg a balance sheet and a profit and loss account.

The following points should be noted:

- Section 393(2) imposes a duty on a company’s auditors to “have regard to” the directors’ duty not to approve accounts unless they are satisfied that they give a true and fair view of the company’s assets, liabilities, financial position and profit or loss. No such requirement was expressly stated in the 1985 Act.
- A medium sized parent company is now required to prepare group accounts. Under the 1985 Act a parent company which was itself a medium sized company, did not have to prepare group accounts.

Advice: This is an important change and you should be aware of the removal of the grouping exemption for medium sized parent companies.

Chapter 5 of Part 15 (sections 415 to 419) contains provisions relating to the directors’ report. These provisions are, in the main, the same as those contained in the 1985 Act (as amended) but the following points should be noted:

All companies except small companies must include a business review in their directors’ report. Section 417 stipulates what must be included in the business review.

Advice: Note that section 417 will come into force on 1 October 2007.

On 20 January 2007 section 463 of the Act came into force. This is an important section which, whilst it states that a director is liable to compensate the company for any loss suffered by it as a result of any untrue or misleading statement in the directors’ report, it also provides a “safe harbour” for directors as a director will only be liable if he knew that the statement was untrue or misleading or was reckless as to whether it was untrue or misleading or he knew that an omission from the statement was a dishonest concealment of a material fact.

The purpose of this safe harbour is to encourage directors to provide information in the directors' report and especially in the business review which is informative. Under the legislation which existed before the 2006 Act there was a tendency for directors to issue generalised or non-specific information in the business review in case it was later found to be untrue or misleading. Under the amended legislation a director will not be liable in these situations provided that he acted honestly and was not reckless.

Section 418 of the Act is a new requirement which provides that where a company has been subject to an audit, the directors' report must contain a statement that as far as the directors are aware, there is no relevant audit information of which the company's auditor is unaware and that each director has taken all the steps he ought to have taken to make himself aware of any relevant audit information and to establish that the company's auditor is aware of that information.

Chapter 6 of Part 15 (sections 420 to 422) contains provisions relating to the preparation of a directors' remuneration statement by quoted companies.

Chapter 7 of Part 15 (sections 423 to 436) contains provisions relating to the publication of accounts and reports. Many of these provisions are similar to those contained in the 1985 Act, but the following should be noted:

Section 424(2) provides that a private company must circulate copies of its accounts to those entitled to receive copies (ie in the main – its members), no later than the end of the period for filing accounts and reports or, if earlier, the date on which it actually delivers its accounts and reports to the registrar.

A public company must circulate its accounts and reports at least 21 days before the date of the relevant accounts meeting.

Sections 426 to 429 deal with the summary financial statement and allow the Secretary of State to introduce regulations to allow companies (including unquoted companies) to provide a summary financial statement instead of full accounts and reports. As at the date of this publication no regulations have been published.

Section 430 provides that a quoted company must ensure that its annual accounts and reports are made available on a website. This section also contains provisions relating to the way in which any such website must be operated.

Chapter 8 of Part 15 (sections 437 and 438) contains provisions relating to the laying of accounts and reports of a public company before general meeting. The important point here is that all public companies (ie both quoted and unquoted) must lay their accounts before a general meeting of the company. Private companies do not have to hold general meetings and so do not have to comply with these sections.

Chapter 9 of Part 15 (sections 439 and 440) contains provisions relating to the approval by members of quoted companies of the directors' remuneration report.

Chapter 10 of Part 15 (sections 441 to 453) contains provisions relating to the filing of accounts and reports. The following points should be noted:

Section 442 has amended the periods allowed for the filing of accounts and reports. These are now 9 months (previously 10 months) for a private company and six months (previously 7 months) for a public company.

Section 443 introduces a new provision defining how to calculate the periods allowed for filing accounts and reports. In general this is the same date the relevant number of months later. So, for example, if the end of the accounting reference period is 5 June, 6 months from then is 5 December. However, as months are of unequal length, there can be confusion as to whether 6 months from say 30 June is 30 December (exactly 6 months later) or 31 December (the end of the sixth month). Under the rule laid down in the Act, 6 months from 30 June will be 31 December. This reverses the "corresponding date rule" laid down by the House of Lords in *Dodds v Walker*.

The sections of the Act that deal with the detailed filing obligations (sections 444 to 447) provide that if an auditor's report is delivered to the registrar, it must state the name of the auditor and (where the auditor is a firm) the name of the person who signed it as senior statutory auditor. This is a new requirement as previous legislation only required the name of the firm to be stated, as opposed to an individual.

Note that the balance sheet filed with the registrar no longer requires the signature of a director, but the name of the person who signed the balance sheet and any director's report on behalf of the board must be stated.

Chapter 11 of Part 15 (sections 454 to 462) contains detailed provisions relating to the revision of defective accounts and reports. These need only be studied in the event of a company requiring a revision of its accounts or reports that have been filed with the registrar.

Chapter 12 of Part 15 (sections 463 to 474) contains supplementary provisions, the most important of which are:

- Section 463 – liability for false or misleading statements in reports (see above); and
- Sections 465 to 467 which set out the requirements for companies to qualify as medium-sized companies.

Audit

As stated above, Chapter 1 of Part 16 of the Act (sections 475 to 484) contains provisions relating to the requirement for audited accounts. There have been no material amendments to existing legislation.

Note that Part 16 of the Act does not come into force until 6 April 2008.

There are two points concerning the auditor's report which should be noted:

- Sections 503 to 506 contain provisions relating to the signature on audit reports. These have been referred to earlier and relate to the fact that the audit report must contain the name of the person signing the report and if the auditor is a firm this must be the senior statutory auditor (as defined in section 504).
- A new offence has been introduced by the Act. Section 507(1) makes it an offence for an auditor to knowingly or recklessly cause an audit report to include any matter that is materially misleading, false or deceptive.

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