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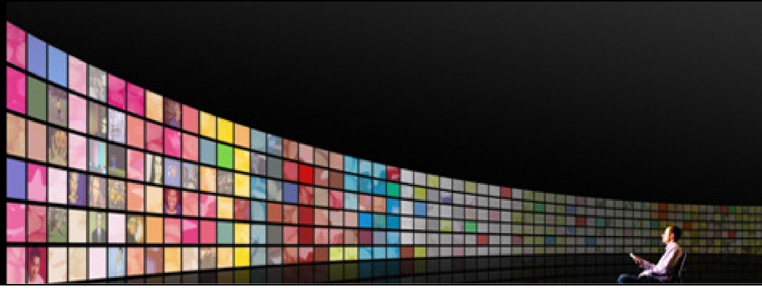
Overview



In this edition we feature a series of articles on one of the biggest proposed changes in company law for some years. The Small Business, Enterprise and Employment Bill currently making its way through Parliament will require the individuals who control UK companies to be publicly disclosed for the first time. There are also draft provisions for the abolition of bearer shares, changes affecting company directors and new corporate administration procedures.

We also consider whether there is a duty to speak up when the other party to a contract is acting under a mistaken assumption – a question considered in the recent *Starbev v Interbrew* case. Our regular Did You Know? feature highlights the new approach taken on the validity of agreements to negotiate in *Emirates Trading Agency v Prime Mineral Exports*. It also looks at new guidance published on equality law and director appointments and includes a reminder of recent changes relating to employee share incentive arrangements.

Contents

Mistaken assumption by another contracting party? When to speak up and when to stay silent

You are in the execution phase of a contract. The other side has stated its view on a matter. You disagree. When do you have a duty to speak out? We look at recent developments in the High Court decision of *Starbev v Interbrew.*

The *Starbev* case highlights issues which can arise where the other side is proceeding on an assumption which you do not accept and you fail to challenge that assumption. Maybe your focus is on other more pressing issues. Maybe you don't want to have an argument at this stage. Or maybe, as in an earlier case, you see an advantage while they proceed mistakenly. In some situations there will be a duty to speak out over your disagreement and, if you don't, you may be left with a position you do not agree with.

How did the issue arise in the *Starbev* case?

The *Starbev* case centred on statements made by the buyer of a brewing business after the purchase had been completed. The statements related to an element of the deferred consideration calculation which depended on the amount the buyer had invested in the transaction. The buyer formally told the seller twice what it considered the investment amount to be. The seller did not challenge this for several years and in fact only did so when the contract provided for the deferred consideration to be calculated and verified, after the on-sale of the business to a new purchaser. The buyer argued that, because of the seller's earlier acquiescence, it had lost the right to challenge the statements (i.e. an estoppel by acquiescence had arisen).

The Judge's decision

The Judge held that, in the absence of a relationship between the parties which implied an obligation of good faith (such as in an insurance context) or partnership or joint enterprise, the court would not impose a duty to speak out in the absence of impropriety. Impropriety could come from the act of staying silent itself - where a reasonable person would expect the party who knows the assumption is wrong, acting honestly and responsibly, to bring the true facts to the attention of the other party.

In *Starbev* the Judge concluded that there was no impropriety and therefore no duty to speak out. The seller had not acted irresponsibly or unconscionably in failing to communicate its doubts about the investment amount at an earlier stage and instead waiting until after the on-sale before verifying the figure in accordance with the provisions of the contract. On the facts the Judge decided that the buyer had known that the seller would probably want to verify the investment amount.

The *Starbev* case contrasts with an earlier shipping case (*The Lutetian*) where an estoppel by acquiescence was held to have applied. There the owners of a vessel purported to withdraw the vessel from charter on the basis that the charterers had tendered an incorrect payment for hire. The owners knew the charterers believed they had paid the right amount but kept quiet, leading the charterers to think, until a very late stage, that there was no objection to their payment calculation. The Judge concluded that it was the owners' duty, acting honestly and responsibly, to disclose their own views about the payment to the charterers. Instead they thwarted the charterers' attempts to discover their views because they were bent on “stage-managing a very profitable withdrawal” (they later re-offered the vessel to the charterers at almost double the original rate).

It is easy to see in this case that the conduct of the owners was unconscionable. Having kept silent on their views as to the correct level of fees to be paid, they were estopped from exercising their right to withdraw.

Practical points

Certainty is almost always preferable to litigation when doing deals. There are a number of ways in which you can improve your position.

- Consider negotiating contractual obligations in relation to key points. Often there is a duty for one side to report on specific matters to the other - consider going further and imposing a contractual duty to speak out if there is disagreement;
- If, during a transaction, something turns out to be important, consider simply asking the other side to confirm your assumption; and
- If you are not able to get confirmation about an issue from the other side, improve your chances of setting up a successful estoppel by acquiescence by being clear and repetitive in your communications. Confirm that you are operating and relying on the assumed basis.

Transparency of UK company ownership: far reaching changes on the way

The Small Business, Enterprise and Employment Bill is currently making its way through Parliament. Of particular importance to UK companies and their shareholders are the provisions dealing with the transparency of company ownership. The proposed changes are far reaching and the Government has indicated its intention to pass the Bill into law in 2015. We summarise the key parts of the draft legislation, its implications and who needs to start preparing for its implementation.

In the summer of 2013, at the UK hosted G8 summit, the Government committed itself to implementing reforms designed to combat tax evasion, money laundering and terrorist financing by improving the transparency of company ownership and control in the UK. Following a consultation, the new Bill proposes the following key measures.

- **A requirement for UK companies to maintain a new, publically accessible register of those individuals with significant control (broadly more than 25%) over its shares or management.** General counsel and company secretaries will need to implement the new rules; beneficial owners will need to consider how their investments in UK companies will be disclosed. See page 6 for our summary of the provisions and their implications.

- **A prohibition on creating new bearer shares and the mandatory conversion or cancellation of existing bearer shares.** Under the proposals, if bearer shares are not converted to registered shares within the limited window of opportunity provided by the legislation, companies will be required to apply to court to reduce their share capital and cancel them. For companies, this will have cost and possibly solvency implications and for the holders of bearer shares, there is the risk of losing the shares and their value if action is not taken within the timetable set out. See page 8 for further details of the statutory timetable for conversion and the consequences of failing to do so.

- **New provisions relating to directors,** including a prohibition on appointing new corporate directors; the automatic termination of existing appointments of corporate directors; and the extension of directors' statutory duties to shadow directors. Companies with corporate directors will need to consider whether any additional individual directors should be appointed and if so, who. See page 10 for more details.

Also included within the new Bill, and of particular interest to company secretaries and those involved in compliance and filing, are the proposed changes to annual return filings, the new ability for companies to keep statutory registers (such as the register of members) at Companies House and changes to statements of capital. We will cover this in greater detail once Companies House procedures and timings become available.

Transparency of UK company ownership: new duties to disclose controlling interests

Many UK companies, and individuals with a controlling interest in them, will be subject to increased disclosure obligations under the proposed new Small Business, Enterprise and Employment Bill.

New duties for companies

If the Bill is enacted, UK companies will be obliged to maintain a publically accessible register (**PSC Register**) of those individuals who, either alone or jointly with others, have "significant control" over the company – "registrable individuals".

Individuals with ***significant control***…

- directly or indirectly ***hold more than 25%*** nominal share capital; or
- directly or indirectly ***control more than 25%*** of the votes at general meetings; or
- directly or indirectly are able to ***control the appointment or removal of a majority of the board****;* or
- actually exercise or have the right to exercise ***significant influence or control*** over the company (*Government guidance on what this will encompass is awaited);* or
- actually exercise or have the right to exercise ***significant influence or control*** over any trust or firm which has ***significant control*** (under one of the 4 criteria above) over the company

As well as being held on the PSC Register, this information will need to be confirmed to Companies House at least every 12 months.

In order to compile the PSC Register, companies will be under a duty to investigate the identity of any person they know to be (or who they have reasonable cause to believe is) a registrable individual, to obtain the required details of that individual and keep that information up-to-date.

Companies will also have the power to make enquiries of any other person where the company knows (or has reasonable cause to believe) that such person either knows the identity of a registrable individual or knows the identity of someone else who knows that information.

New duties for beneficial owners of shares

Individuals who know, or ought reasonably to know, that they have significant control over a UK company, will have an obligation to inform the company of their interest (and any changes to it) where the company has not already requested that information. In addition, failure to respond to a company's enquiries will give the company the ability (without a court order) to disenfranchise and impose other restrictions on the relevant shares. Ultimately, where the company is unable to identify the beneficial owners of the shares, it will be able to apply to court for an order to sell the affected shares.

Exemptions

- Companies under an obligation to report under DTR 5 e.g. LSE Main Market and AIM companies, do not need to maintain a PSC Register. Some other companies (for example, UK companies listed overseas which are subject to a similar disclosure regime to the DTRs) may also be excluded by regulations.

- PSC Registers will not need to be repeated at every level in a corporate chain. Where a company or other legal entity (as opposed to an individual) has significant control over a company, then provided that the legal entity is itself under a disclosure obligation (e.g. to maintain a PSC Register or under DTR 5) it will be sufficient simply to identify that "relevant legal entity" in the PSC Register of the company concerned. However, the Bill contains anti-avoidance provisions so that inserting an entity which is outside the scope of the new rules in the chain of ownership will not prevent the UK company having to look past those entities and disclose the individuals with ultimate control.

- Where there is a risk of violence or intimidation, regulations are expected to exempt companies from the requirement to allow public access to the PSC Register (see *What is still outstanding?* below).

What is still outstanding?

There is still a lot of detail to be finalised and the Bill provides for regulations to be made in various areas to fill in these gaps. In particular, we are waiting for:

- clarification as to whether LLPs will be required to maintain a PSC Register – although the Government indicated earlier that LLPs and possibly Scottish Limited Partnerships (as they are separate legal entities) would be included in the rules, they are not mentioned in the new Bill;

- guidance on how "significant influence or control" will be interpreted;

- regulations giving details of how each registrable individual's interest is to be recorded in the PSC Register, possible exemptions from the requirement to keep a PSC register and exemptions from the obligation to make the register (or certain information on it) publically available.

Implications

- Individuals with significant control over UK companies who are legitimately concerned about confidentiality, should be aware that their details and arrangements will usually be made public.

- New internal processes will be required to enable companies to identify registrable individuals and relevant legal entities and maintain the PSC Register. Company secretaries and general counsel will need to adopt procedures for gathering and maintaining the information for the PSC Register.

- The rules currently only apply to UK companies, not to foreign companies operating in the UK, and this "loophole" has led to criticism from some commentators. However, the Government has pledged to lobby other jurisdictions to implement similar rules (to avoid the UK being at a competitive disadvantage as a result of the new disclosure requirements) and the EU is expected to introduce similar measures if proposals for a fourth money laundering directive are adopted.

- Criminal sanctions will apply to companies and their officers, and to individuals, for non-compliance.

Transparency of UK company ownership: proposed abolition of bearer shares

Bearer shares will be outlawed if the Small Business, Enterprise and Employment Bill is enacted in its current form. Action will need to be taken by both companies with outstanding bearer shares and the holders of those shares, who should monitor the progress of the legislation and factor the changes into their arrangements.

The key provisions

If the proposals are implemented as currently drafted:

- the issue of new bearer shares will not be permitted;
- holders of bearer shares will have the right to surrender the warrants for conversion into registered shares during a strict 9 month surrender period (see the flow chart below);
- companies will be obliged to apply to court to cancel bearer shares if they are not surrendered within the surrender period; and
- if cancellation is required, companies must also pay into court the amount of share capital (nominal and premium) paid up on the bearer shares to be cancelled plus any accrued dividends – this can be claimed by the bearer of the warrant for up to three years following cancellation provided the holder can show that the failure to exercise the right of surrender was due to "exceptional circumstances". Unclaimed monies will go to the Government.

Implications

- Although bearer shares are not often used in UK companies now, they have been used historically for structuring and tax planning.
- Companies will want to avoid applying to court for the cancellation of any bearer shares, given the costs involved and the fact that companies will have to fund the payment into court of the amount of share capital to be cancelled. This is particularly true of companies where the reduction in share capital might cause solvency issues.
- Public companies with bearer shares should pay particular attention to the amount of share capital attributable to the bearer shares because any cancellation of bearer shares which results in the share capital dropping below the minimum required by the Companies Act 2006 may force the company to re-register as a private company.
- Holders of bearer shares should monitor the progress of the legislation and begin discussing conversion of their shares into registered shares now, to avoid the risk of losing both the shares and their value.
- Company secretaries and general counsel of relevant companies should discuss the surrender and conversion of bearer shares with warrant holders sooner rather than later, as the Bill requires detailed procedures to be followed within a given timetable – see the flow chart below.

Commencement Date: the legislation comes into force

Within one month of the Commencement Date

Company must send a first notice to holder(s) of bearer warrants detailing:

- the holder's right to surrender the shares for conversion and the fact that the right is only exercisable for 9 months from the Commencement Date
- the consequences of not surrendering within 7 months of the Commencement Date
- the consequences of not surrendering within 9 months of the Commencement Date

7 months from the Commencement Date

Unsurrendered bearer shares will be disenfranchised …

- any subsequent transfer of the share warrant will be void
- all rights attaching to the shares specified in the warrant will be suspended (including rights to vote and receive dividends)
- the company must pay all subsequent dividends and other distributions attributable to the bearer shares into a separate bank account (money can be paid out to the warrant holder on surrender of the warrant)

Before the end of 8 months from the Commencement Date

Company must send a second notice to the holder(s) of bearer warrants detailing:

- the holder's right to surrender the shares for conversion and fact that the right is only exercisable for 9 months from the Commencement Date
- the consequences of not having surrendered the warrants within 7 months of the Commencement Date
- the consequences of not surrendering within 9 months of the Commencement Date

9 months from the Commencement Date

End of the Surrender Period: bearer warrants can no longer be surrendered for conversion into registered shares

Within 3 months following the end of the Surrender Period

Company must apply to court to cancel the bearer shares:

- company must apply to court for an order cancelling any outstanding warrants and the shares covered by them
- company must give notice of the application to the holder of the warrants and to the Registrar of Companies

Transparency of UK company ownership: provisions relating to directors

The Small Business, Enterprise and Employment Bill contains a number of provisions relating to directors. Some of the changes, for example the ban on corporate directors, are part of the Government's drive for transparency in corporate management and control. Others, for example the ability of the court to disqualify a director following misconduct abroad, are designed to increase trust in UK companies by improving the accountability of directors for misconduct.

Abolition of corporate directors

The draft Bill prohibits the appointment of new corporate directors and provides that the appointments of existing corporate directors will automatically cease 12 months after the new law comes into force. Some limited exceptions to the general prohibition are expected to be made by regulations, although these are likely to be narrowly defined (for example, limited to subsidiaries in large corporate groups).

The impact of these provisions is likely to be largely administrative and should not pose a problem for most companies as all companies have needed at least one natural person on the board since October 2008 (or October 2010 in some limited transitional cases). However, if implemented, the changes are likely to result in an increase in the number of individuals taking on the duties and responsibilities of directors. Companies will need to identify appropriate individuals willing to take on the role. The Government's response to the consultation on this point also indicated that it was considering extending the prohibition on corporate directors to LLPs. This has attracted much criticism, on the basis that a member of an LLP is not equivalent to a director of a company. As yet, nothing in the Bill extends these provisions to LLPs.

Extension of directors' statutory duties to shadow directors

The Bill seeks to extend the liability of shadow directors (a person, in accordance with whose instructions, the board of a company is accustomed to act) so that, to the extent possible, they reflect the statutory duties applicable to directors. However, it seems likely that further clarification of how these duties might be applied will be necessary and the Bill specifically envisages that regulations may be required to deal with this. Where management structures involve appointed or nominee directors, it will be worth keeping a watching brief on these changes.

Provisions relating to the accountability of directors for misconduct

The Bill seeks to extend the accountability of directors in a number of ways. In particular, a new provision will allow disqualification proceedings to be brought against directors who have been convicted of certain overseas offences connected with establishing and running companies. In addition, in certain circumstances where a director has been disqualified for conduct caused by his having followed the instructions of another person, the court will also be able to disqualify the individual who exerted the "required influence" over the director. The Bill also expands the matters to which a court must have regard when considering disqualification.

Did you know…?

……….that the Commercial Court has recently held that a time limited obligation to engage in "friendly discussion" before proceeding to arbitration was enforceable? In a departure from long-standing case law to the effect that agreements to negotiate are void for lack of certainty, the Court held that the clause was indeed enforceable and that the obligation constituted a condition precedent which had to be satisfied before the parties could start arbitration proceedings.

The clause in *Emirates Trading Agency LLC v Prime Mineral Exports Private Ltd* provided that: *"11.1 In case of any dispute or claim arising out of or in connection with or under this [contract]… the Parties shall first seek to resolve the dispute or claim by friendly discussion. Any party may notify the other Party of its desire to enter into consuLTCion [sic] to resolve a dispute or claim. If no solution can be arrived at in between the Parties for a continuous period of 4 (four) weeks then the non-defaulting party can invoke the arbitration clause and refer the disputes to arbitration."* The Judge attached significance to the use of the word "shall" in the clause, which he concluded rendered the obligation mandatory (as opposed to the provision for notification which was held to be voluntary, on the basis of the use of the word "may") and also to the constraining time limit of four weeks, which he considered added to the certainty of the clause. He rejected the claimants' suggestion that the clause required the parties to engage in four weeks of discussions, holding instead that the proper construction was that four weeks had to elapse before the parties could initiate arbitration proceedings.

It remains to be seen whether the Court's approach will be followed in future cases, or whether higher courts will revert to the previous assumption that agreements to negotiate are void for uncertainty. For more information, see our article here.

……….that, as companies respond to pressure to recruit more women to their boards, the Equality and Human Rights Commission has issued timely guidance on the steps companies can take within the boundaries of equality law. The guidance looks at how unlawful discrimination can occur in the recruitment process, the limited circumstances in which gender can be taken into account, the lawfulness of female only shortlists and the liabilities that can arise where executive search firms or recruitment agencies are involved. The guide is intended for companies, nomination committees, search firms and recruitment agencies and can be found here.

……….that the Finance Act 2014 has now received Royal Assent, meaning that the second major set of changes to employee share incentive arrangements in successive years is now on the statute books. For a summary of the key changes, see our article here.

The information contained in this update is intended as a general review of the subjects featured and detailed specialist advice should always be taken before taking or refraining from taking any action. If you would like to discuss any of the issues raised in this article, please get in touch with your usual Olswang contact.

About Olswang's corporate team

Our international corporate group advises a range of clients, from large listed companies to small start-ups. In 2013 we completed over 160 deals with an aggregate value of over £6.5bn.

Our recent international M&A deals

- **Belgacom SA** – advised on the sale of the entire issued share capital of Belgacom's French IT services unit Telindus, a French market leading ICT Services Company and leading integrator for cross-border ICT projects, to Vivendi Group and its subsidiary SFR. This deal involved both our Paris and Brussels team.
- **ITE Group Plc** —advised ITE Group Plc, on its acquisition of 50% of the entire issued share capital of PT Debindo Unggul Buana Makmur, the Indonesian construction, airport and building materials trade show and conference organiser, from its founding shareholders.

Awards and rankings

- **The Lawyer** – ranked 6th for FTSE AIM 100 clients in Q2.
- **Bloomberg** – ranked in the top ten by deal count for UK M&A and the top 20 by deal count for European M&A in 2013.
- **Legal 500** – ranked Tier 1 for mid-market M&A, 2013.
- **M&A International Global Awards** – TMT law firm of the year, Germany 2013.
- **Acquisition International Finance Awards** – UK M&A Advisor of the Year 2014.

About Olswang

Olswang is a leading international, full service law firm famous for being industry experts in technology, media and telecoms sectors. Headquartered in London, Olswang has an international presence spanning Belgium, Germany, France, Singapore, Spain and the UK.

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