

CORPORATE TRANSPARENCY AND ACCOUNTABILITY UPDATE

In our September 2013 Corporate & Commercial Briefing we reported on and discussed the UK Government's proposals to improve corporate transparency and public confidence in the financial sector.

On 21 April 2014, the Department for Business, Innovation & Skills (BIS) published the UK Government's response to its discussion paper of July 2013 entitled "Transparency & Trust: Enhancing the Transparency of UK Company Ownership and Increasing Trust in UK Business" and confirmed its intentions to proceed with the majority of the consultation proposals. The response is the result of focus groups and roundtable discussions with companies and interested groups, over 300 direct responses to the discussion paper itself and surveys to inform analysis of the costs and benefits of the proposals and impact assessment. According to Vince Cable MP, Secretary of State for BIS "*trust is essential to every commercial transaction*" and "*transparency and accountability are both essential for trust*". Indeed, a common theme runs through BIS' response: transparency and accountability.

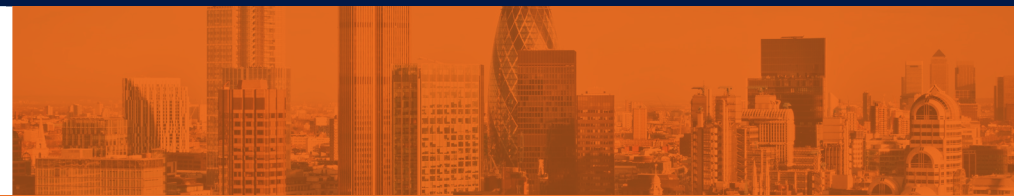
This Corporate & Commercial Briefing provides a brief overview and highlights some of the implications of the proposals that will now be adopted and implemented by the UK Government.

Transparency

Beneficial ownership

Currently, the registered office of a UK company must keep registers of its directors and direct shareholders (i.e. those who "legally" own the shares), and must make certain filings of this information on the public register maintained by Companies House. A UK company has no duty to enquire as to whether the shares are held on trust for another person, nor does it, if the shares are held by another legal entity, such as an overseas company, have any duty to enquire as to the owners of that other entity. It need only deal with its direct shareholders.

Following the recent proposals, the UK Government aims to launch a publically accessible new central registry of company beneficial ownership information and will require companies to identify "qualifying beneficial owners". The UK Government will adopt the definition of beneficial ownership used in the anti-money laundering context, which defines a qualifying beneficial owner as someone with an ultimate interest in 25% of the shares or voting



rights of a company or an “individual who otherwise exercises control over the management of the company”. Contrast this with trusts, where only the trustee’s (and not the beneficiary, settlor or protector of the trust) details will need to be registered as the qualifying beneficial shareholder.

Since it is not yet clear what tests would be applied to assist with identifying when an individual would be otherwise exercising control over management, it could potentially make any disclosure obligation burdensome (such as minority protections in shareholders’ agreements or in articles of association).

The UK Government intends to replicate the provisions of Part 22 of the Companies Act 2006, which applies to public companies, to assist private companies to identify their beneficial owners. Companies will now be required to update the information in their register if they know or have reasonable cause to believe that there has been a change to its beneficial ownership.

The UK Government has taken the view that the Companies House public register should include information above and beyond that contained in the companies register, including the beneficial holder’s full name, month and year of birth, nationality, country or state of residence, service address and shareholding. BIS is currently considering which UK and overseas authorities should have access to the protected information.

Under the UK Government’s slogan “check, notify changes if necessary and confirm”, there will be an annual requirement to confirm the accuracy of the information held, with criminal sanctions for breaches. The new rules will be applicable to all companies and limited liability partnerships, with the exception of Main Market listed companies subject to the Disclosure and Transparency Rules (or equivalent requirements).

Bearer shares

The new proposals abolish bearer shares and prohibit the creation of new bearer shares, which the UK Government states “*permit a level of opacity incompatible with our ambitions for corporate transparency*”. The ban will come into force two months after royal assent. The effect is to encourage bearer shareholders to surrender their warrants (within a period of nine months) with a view of converting them to registered shares.

Once the surrender period has expired, companies with remaining bearer shares would have three months within which to apply to court for the shares to be cancelled. As a failsafe, bearer shareholders who were not able to convert their shares in time will be given three years to apply to the court for the value held on trust if they can show exceptional circumstances as to why they were unable to surrender their shares.

Corporate directors

Subject to certain exceptions (charities and group structures, including large private or listed companies), corporate directorships will be banned. There will be a one-year transitional period for existing companies, with the UK Government considering whether the ban should also apply to limited liability partnerships. Currently, the Companies Act 2006 requires companies to have at least one natural person as a director.

Accountability

Directors’ accountability

The UK Government proposes to allow causes of action that arise on an insolvency (e.g. for fraudulent or wrongful trading) to be assigned to another party to pursue, in order to increase the chances of action being taken against offending directors for the benefit of creditors. Furthermore, the proposals seek to empower the Secretary of State to apply to the court for a compensation order against a disqualified director

(and empower the Insolvency Service to accept a compensation undertaking from such directors) where creditors have suffered identifiable losses from their misconduct.

The UK Government is also considering explicitly applying the directors’ statutory duties to shadow directors, as presently, the definition of a shadow director is restricted to those who control all or a majority of the directors on a company board.

Directors’ disqualification

The Government intends to:

- Amend the Company Directors Disqualification Act 1986 by replacing Schedule 1 (which sets out matters determining unfitness) with “*new, broader and more generic provisions*” for the court and the Insolvency Service.
- Increase the time limit for bringing disqualification proceedings in insolvency cases from two years to three years.
- Enable the courts to take overseas misconduct into account when presiding over misconduct hearings (including empowering the Secretary of State to disqualify an individual in the UK where that individual has been convicted of a corporate criminal offence abroad).

There will be greater information sharing and cooperation, with the Insolvency Service able to share investigative information with other regulatory or enforcement bodies, with a view to promoting effective working between sectoral regulators (such as the Financial Conduct Authority and the Prudential Regulation Authority). This aims to build on current best practice and to develop a system where company law enforcement is fully integrated.



Improving public perception

The UK Government also recently responded to BIS' consultation paper "Red Tape Challenge: Company Filing Requirements". The aim of that policy is to improve the accuracy and integrity of the public register, whilst also simplifying the current filing requirements. Proposals include:

- Allowing companies more flexibility to confirm whether their company information is correct and complete at any point in a year.
- Giving private companies the option of not keeping any, or all, of the following registers:
 - Register of directors.
 - Register of directors' residential addresses.
 - Register of secretaries.
 - Register of members.
 - The proposed register of beneficial ownership.
- Removing the requirement for a company's statement of capital to list the amount unpaid and paid up on each share (showing only the aggregate amount unpaid).
- Implementing the EU Accounting Directive requiring companies with subsidiaries to list all of these in one place (the accounts).
- Removing the requirement for companies to file a "consent to act" for newly appointed directors and company secretaries, and replacing this with a requirement for the company to make a statement of truth that the person has consented to be a director/company secretary.

For many companies, whether or not to opt out of keeping the company registers will be a key decision. Opting out will reduce administrative burden (in that the company will no longer have to separately update its own

registers), but companies will still have to notify Companies House in respect of information for the public registers.

Those who have structured their investments in the interests of privacy should keep an eye on the proposals as they will not necessarily wish the extent of their interests or wealth to become public. For example:

- International investors and individuals who invest in diverse businesses.
- Those in the public who own their homes and other assets through companies to avoid intrusion into their private lives.
- Those who employ trust structures (such as families in business) and other means of separating management decision-making from the economic benefit of owning a share in the family business.

Proposals not adopted

Banks and other financial institutions will be pleased to know that, of the many proposals initially put forward by BIS, the UK Government has concluded that there will be no:

- Amendment of directors' general statutory duties to introduce a primary duty for bank directors to promote financial stability over the interests of their shareholders.
- Extension of powers to sectoral regulators' powers to enable them to bring directors' disqualification proceedings.

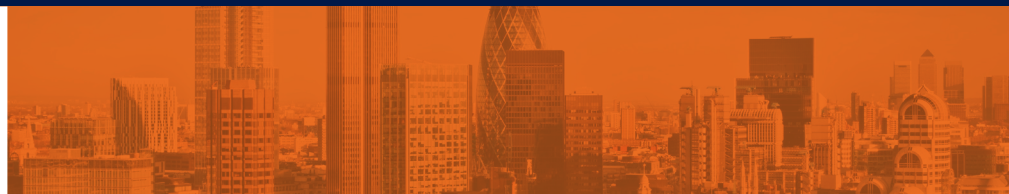
With respect to nominee directors, the UK Government is also not intending to follow up with its proposal for a new Companies House register of nominee directors and their appointees. The UK Government now intends to increase directors' awareness and is considering whether any individual controlling one or more directors should be made legally liable and subject to directors' general statutory duties.

Many of the changes will require primary and secondary legislation and are linked to developments in Europe. Whilst the UK Government intends to introduce legislation as soon as Parliamentary time allows, changes are unlikely to be imminent as Parliamentary time is likely to be limited before the UK general election in 2015. The UK Government is, however, intending to implement the registry of beneficial ownership as soon as practicable, once the necessary legislation is in place and will consider transitional arrangements for existing companies.



Some companies may be put off by the increased transparency that the proposals bring, but on the whole I think this will be good for the UK's reputation as a sophisticated economic investment location that moves with the times.

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