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The Small Business, Enterprise and Employment Bill

The Small Business, Enterprise and Employment Bill is currently making its way through Parliament, with the report and third reading stages expected to take place in the Commons on Tuesday 18 November and Wednesday 19 November 2014 and the Government intending to pass the Bill into law in 2015.

The Bill is intended to reduce the barriers that currently hamper the ability of small businesses to innovate, grow and compete and of particular relevance to UK companies are the provisions dealing with the transparency of company ownership. The proposed changes are likely to be extensive, but we set out below some of the key considerations for small business owners that arise from the Bill as currently drafted.

Publically accessible register of those individuals with significant control

If the Bill is enacted as currently drafted, UK companies will be required to maintain a publically available register of all individuals who either alone or jointly with others have "significant control" over the company, to be known as a PSC Register. Individuals with "significant control" will be those who:

- 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; 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 four criteria above over the company.

Further guidance will undoubtedly be required, not least in connection with how "significant influence or control" is to be interpreted. However, individuals who satisfy the above characteristics are to be considered "registrable individuals".

Under the Bill, the identity of all registrable individuals is to be held on the PSC Register and confirmed to Companies House at least every 12 months. What is not yet clear, and will also likely require further regulation, is the detail of how each registrable individual's interest is to be recorded in the PSC Register and what, if any, exemptions are likely to apply in relation to the obligations to keep a register and to make it publically available. It may therefore become necessary for individuals and companies to prepare for, or take into account, the fact that their details and arrangements will be made public and this will be particularly sensitive where there are individuals who are legitimately concerned about confidentiality.

What is clear from the current draft is that the Bill imposes an obligation on the company to investigate the identity of any person it knows to be, or has reasonable cause to believe is, a registrable individual. There will also be an obligation on the company to obtain all necessary details in connection with that individual and to keep the information up-to-date. In addition, it is also intended that there will be a reciprocal obligation on individuals who know, or ought reasonably to know, that they have significant control over a UK company. The duty imposed on such individuals is twofold: they must (1) respond to any enquiries made by the company in connection with their status as a registrable individual; and (2) they must inform the company of their interest and any changes to it if the company has not already requested the information.

Opinion appears divided at the Committee stage as to whether the introduction of the PSC regime, as currently drafted, will be a positive change for UK companies. Whilst some commentators suggest the complexity of the regime means that transparency would come at the cost of additional regulatory burdens, other sectors draw comparisons with the recently introduced self-policing provisions in money laundering legislation and point to the benefits of law enforcement of lifting the 'veil' of incorporation by shell companies. What is clear, in practical terms to UK companies and those who control them, is that new internal processes will have to be implemented to identify all relevant registrable individuals and to maintain a PSC Register. In terms of what this will cost to UK business, the Government's impact assessment estimates that the regime will cost some £97 million but is to be borne by 3 million companies. It is the Government's stance that the cost of the regime is not disproportionate to achieve the advantage of transparency and trust in UK business.

Prohibition on bearer shares

Bearer shares are a type of freely transferable security with which participation in a company can only be demonstrated by possession of the share certificate. The regime of bearer shares has been heavily criticised in recent years due to the use of such shares for illegal activity such as money laundering and tax avoidance. This is because there is no need for any legal processing to change the ownership of bearer shares and because the transfer of the title is not documented, so there is no evidence of transmission and therefore there will not be a taxable event to tax. In addition, such shares allow the owners of a company to remain almost completely anonymous and a change in the shareholding is a completely confidential act.

One of the overriding purposes of the Bill is to ensure that the UK is seen to be a trusted and fair place to do business. It is for this reason that regulations have been proposed to increase the transparency around who owns and controls UK companies and to deter illegal activity. Under the proposals, bearer shares are to be outlawed and, if passed into law, this will have serious consequences for all companies with such shares in issue.

If bearer shares are not converted to registered shares within the limited window of opportunity provided by the legislation (see flowchart below), companies will be required to apply to court to reduce their share capital and cancel the shares. This will have cost and possible solvency implications for the company and there is the risk to holders of bearer shares of losing the shares and their value entirely if action is not taken within the timetable set out. Action will therefore need to be taken by both companies and the holders of bearer shares, so all involved would be well advised to keep up to date with the progress of the Bill and factor the necessary changes into their arrangements.

Commencement Date – the legislation comes into force.

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Within 1 month of the Commencement Date – the company must send a first notice to holders of bearer shares detailing:

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

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After 7 months have passed from the Commencement Date:

- un-surrendered bearer shares will be disenfranchised;
- all rights attached to the shares will be suspended (including rights to vote and receive dividends);
- the company must pay all future dividends and other distributions attributable to the bearer shares into a separate bank account (the funds can then be paid to the holder if/when the share certificate is surrendered)

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Before the end of 8 months from the Commencement Date – the company must send a second notice to the holders of bearer shares with the same detail as sent under the first notice.

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9 months from the Commencement Date – the end of the surrender period, after which bearer shares cannot be surrendered in exchange for registered shares.

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Within 3 months following the end of the Surrender Period – the company must apply to Court to cancel the bearer shares and must give notice of the application to the holders of the shares and to the Registrar of Companies.

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

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surrender the warrants for conversion into registered shares during a strict 9 month surrender period, 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 will also have to pay into court the amount of share capital (nominal and premium) paid up on the bearer shares to be cancelled plus any accrued dividends. Any monies paid into court can be claimed by the holder of the bearer share certificate 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", but all unclaimed monies will go to the Government.

New provisions relating to directors

The Bill contains several provisions relating to directors, as part of the Government's drive for transparency and trust in UK companies. For example, the changes include a ban on corporate directors, the ability of the court to disqualify a director following misconduct abroad and proposed changes to company secretarial requirements. Though further detail will have to be provided in due course, the following summary of provisions should be noted.

Abolition of corporate directors

The Bill as currently drafted prohibits the appointment of new corporate directors and states that appointments of existing corporate directors will automatically expire 12 months after the Bill becomes law. There are likely to be some limited exceptions to the general prohibition, which are to be dictated by the Secretary of State, but it is expected that any such exceptions will have very limited application in practice. At present, it is expected that approval of a non-natural director will be subject to the approval of a regulatory body, though the identity of that body remains an unknown.

These provisions should not cause too much difficulty for most companies because all companies have been required to appoint at least one natural person to the board since October 2008. In practice, the scope of the changes are likely to be largely administrative. However, it seems likely that the number of individuals taking on the duties and responsibilities of directors is set to increase and companies will need to identify appropriate individuals who are willing to take on the role.

Extension of directors' statutory duties to shadow directors

The Bill seeks to extend the liability of shadow directors (a person who is not a named director but in accordance with whose instructions the company is accustomed to act) so that the obligations more closely reflect those applicable to directors. In practice, this change will simply make the role of being a shadow director more onerous, but it is likely that further clarification and regulation will be needed before the Bill is passed, not least because the Bill seeks to amend the legal definition of what a shadow director is.

Provisions relating to the accountability of directors for misconduct

In relation to disqualification of directors, the draft Bill seeks to expand the matters to which a court must have regard when considering disqualification and extend the accountability of directors. For example, the Bill provides that disqualification proceedings can be brought against UK directors who have been convicted of misconduct abroad. The scope of the court is further extended so that where a director has been disqualified for conduct caused as a result of the director following instructions from another person, the court will be able to disqualify the individual who exerted the "required influence" over the director.

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