



ARTICLES OF ASSOCIATION - TIME FOR AN UPGRADE?

A company's articles of association (**articles**) are a set of rules which govern the internal affairs of the company and form the basis of a statutory contract between the shareholders of a company and the company itself. Every company must have a set of articles but keeping these up to date can often fall by the wayside in favour of more demanding business issues. This note summarises the possible consequences of having out of date articles and the benefits of replacing them.

TYPES OF ARTICLES

A private company limited by shares will usually have one of two types of articles in place:

- 1 Articles which incorporate in whole or in part the default articles under the Companies Act 1985, known as **Table A Articles**; or
- 2 Articles which incorporate in whole or in part the model articles set out in the Schedules to the Companies (Model Articles) Regulations 2008 (SI 2008/3229), known as **Model Articles**.

The Model Articles are designed to follow the Companies Act 2006 (**Act**) and have been drafted to reflect key concerns of small owner managed businesses. They also constitute the default provisions for companies limited by shares incorporated on or after 1 October 2009. This means that, if the articles you adopt are silent on a matter, the Model Articles will apply for that matter.

Where a company was incorporated before 1 October 2009, you will need to take some action in order to incorporate the Model Articles into its existing articles.

Where a company has Table A Articles, it may be subject to increased regulatory burdens when compared with the Model Articles. The directors could find themselves misled by discrepancies between the Act and more historic legislation, which may even result in the company unknowingly committing an unlawful act. Generally, out of date statutory references will not present a legal problem due to transitional legislative provisions which substitute out of date statutory references. However, it does reduce costs when legal advisors are reviewing articles if the statutory references are up to date as the articles are inevitably clearer and easier to interpret.

POSSIBLE INCONSISTENCIES BETWEEN TABLE A ARTICLES AND CURRENT LAW

As mentioned, there have been changes in legislation which could mean that, despite following the rules and restrictions set out in a company's articles, certain procedures could be challenged. This is because the Act has made various amendments to matters covered by the articles which could, subject to some exceptions, override what a company's articles say. Some examples of this are:

- **Shareholders' resolutions** - Provisions which provide that any shareholders' resolutions to be passed by written resolution must be signed by all members are now ineffective. Any written resolutions of the shareholders which purport to follow this provision in a company's articles will therefore now be invalid. Instead, the provisions set out in the Act apply which require the holders of at least 75% of shares to pass a special resolution and the holders of in excess of 50% of shares to pass an ordinary resolution.
- **Casting vote of the chairperson** – Unless a company's articles, which were in force before 1 October 2007, give the chairperson of a shareholders' meeting a casting vote, the chairperson will no longer have that right. This means that any shareholders' resolutions which are passed using a chairperson's casting vote (without the associated express provision in the company's articles) could now be invalid.
- **Rights of proxies** – Recent legislation has enabled a proxy (i.e. a person appointed by a shareholder to attend a shareholders' meeting on his behalf) to attend, speak and vote at shareholders' meetings, whether by way of a show of hands or on a poll. Table A Articles often say that proxies will only be allowed to vote on a poll, however, if a company were to prevent a proxy from voting on a show of hands, it could be faced with a claim that it is in breach of the Act.
- **Terminating a director's appointment when a mental health court order is made** – Whilst not invalid, recent legislation has suggested that the inclusion of such a provision is discriminatory and therefore that companies that rely on it could be subject to a discrimination claim. You should therefore consider removing such provisions from the articles.

ADVANTAGES OF MODEL ARTICLES

The Act contains certain more relaxed provisions which will automatically apply to companies incorporated on or after 1 October 2009, unless the articles expressly state otherwise. Companies incorporated before this date may wish to adopt Model Articles to benefit from such provisions. Examples include:

- **Electronic communications** – Board members and shareholders can now communicate electronically, even if a company's articles are silent on this point.
- **Unlimited objects** – A company now has unrestricted objects (unless otherwise stated in the articles). This means there are no restrictions on what the company has the power to do. It is worth noting that in order to remove a company's objects from Table A Articles, a form CC04 must also be filed with Companies House, or the change will not be effective.
- **No authorised share capital** – A company is no longer required to be subject to an authorised capital limited.
- **Directors' authority to allot shares** – Whilst the general rule remains that the directors of a company must have authority to allot shares where a company only has one class of shares, the board of directors will automatically be authorised to allow new shares of that share class without obtaining shareholder approval (subject to any provisions to the contrary in the articles). It is, however, worth noting that where a company has more than one class of shares in issue there is still a requirement that the directors are authorised to allot shares.
- **Change of name** – A company can now change its name other than by way of passing a special resolution, for example, by passing a resolution of the directors.

- **Notice period for shareholders' meetings** – The minimum notice period for shareholders' meetings for a private company has been reduced to 14 days (or such longer period as the articles may specify) from 21 days.
- **Company secretary** – A private company is no longer required to appoint someone as a company secretary, though it is of course not prohibited from doing so.
- **Annual general meetings (AGMs)** – AGMs are not optional, unless a company's articles require otherwise.
- **Statutory pre-emption rights on the allotment of shares** – Whilst the general rule remains that, when a company allots new shares it must offer them pro rata to the existing shareholders, the articles can now, within certain limits, empower the directors to allot shares as if this rule did not apply. Table A Articles will also contain references to statutory provisions which have now been repealed, so it is worth replacing these references with the modern equivalent.
- **Annual buy back authority** - A private limited company is now allowed to purchase a small amount of its own shares out of capital (rather than profits) up to an annual limit, provided it is authorised to do so in its articles.
- **Treasury shares** – A company that has purchased its own shares out of distributable profits can now hold the shares in its own name, rather than cancel the shares immediately. Such shares are then available for transfer or sale by the company in the future, so gives the company flexibility. The articles do not need to allow for treasury shares, but they should not contain, for example, a requirement for bought back shares to be cancelled. This would effectively prohibit the holding of treasury shares.
- **Extraordinary resolutions and general meetings** – The concepts of extraordinary general meetings and extraordinary resolutions are not used in the Act or the Model Articles. Whilst such provisions are still effective, you may want to consider removing them.

Whilst not a legislative change, you may also wish to remove any provisions which require directors' to retire by rotation.

YOUR OPTIONS

Unless there are extraordinary circumstances, we would always recommend replacing Table A Articles with Model Articles. It is also usually advised to adopt a whole new set of articles, rather than make specific changes to existing ones. To do so, the company would need to obtain shareholder approval to adopt new articles of association by way of special resolution (i.e. the holders of at least 75% of shares). You may choose to adopt the Model Articles wholesale, or ask your solicitors to draft a more bespoke set of articles which incorporate provisions from the Model Articles, but also allow for practices that are specific to the company to be included.

KEY CONTACTS

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