



## The 2009 annual report and AGM

Hot topics



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## **Part 1 – Introduction**

### **Scope of this guide**

This guide outlines hot topics you will need to bear in mind in planning your 2009 annual report and AGM. In particular, we discuss two pieces of legislation that affect periodic financial reporting and AGMs in significant ways – the UK Companies Act 2006 and the EU Shareholders' Rights Directive.

This guide is focused on UK-incorporated listed companies. Where it refers to a 'company' it means a listed company, unless we state otherwise. It is not an exhaustive description of the law or practice applicable to periodic financial reports or AGMs. It states the position as at 30 January 2009.

### **Implementing the final provisions of the Companies Act 2006**

The Companies Act 2006 (the 2006 Act) received Royal Assent on 8 November 2006. More than half of the 2006 Act's sections are now in force, including most of those that affect shareholders' meetings and financial reporting. The remaining sections will be brought into force on 1 October 2009. The final (eighth) commencement order (the Order) sets out how these final sections apply to companies already incorporated on 1 October 2009. The parts of the Order that affect AGMs are discussed in Parts 3 and 4 of this guide.

The Department of Business, Enterprise and Regulatory Reform's (BERR) June 2008 consultation document set out proposals for dealing with the practical changes to Companies House systems needed for final implementation of the 2006 Act. These arrangements may have a significant effect on new incorporations and the filing of returns at Companies House in the first week of October 2009. As far as possible, it will be advisable to avoid incorporating a company around 1 October 2009.

The Order and consultation document are available at [www.berr.gov.uk/bbf/co-act-2006/draft/page40411.html](http://www.berr.gov.uk/bbf/co-act-2006/draft/page40411.html).

Some of the 2006 Act's requirements apply only to 'quoted' companies. A quoted company is, broadly, a company whose shares are officially listed in a European Economic Area (EEA) state or admitted to dealing on the New York Stock Exchange or Nasdaq.

### **Implementing the EU Shareholders' Rights Directive**

Some companies will have to consider making further changes to their articles of association and the way they run shareholder meetings as a result of the implementation of the EU Shareholder Rights Directive (the Directive) in August 2009. Companies that were planning changes to their articles to reflect the final implementation of the 2006 Act may decide to delay these changes and make changes at the 2010 AGM to reflect the Directive's requirements. See Part 3 for more details.

The Directive applies to 'traded' companies – ie companies incorporated in the EU whose voting shares are traded on a regulated market in the EEA.

The government has issued a consultation paper setting out its proposals and draft implementing legislation (the Draft Regulations). Because it is not proposing to publish a summary of responses to its consultation paper until the end of April 2009, many companies will be left in the difficult position of having to decide the approach to adopt for their 2009 AGMs before the Draft Regulations are finalised.

The government intends that the Draft Regulations will come into force on 3 August 2009.

The consultation paper and the Draft Regulations are available at [www.berr.gov.uk/files/file48662.pdf](http://www.berr.gov.uk/files/file48662.pdf). Responses were requested by 30 January 2009.

The Directive sets minimum standards for notices of shareholders' meetings and documents available before the meeting; shareholders' rights to add items to the agenda and table resolutions; shareholders' rights to participate, ask questions and vote at meetings; provisions on proxies; and provisions on voting and voting results. It also increases the notice required for general meetings other than AGMs to 21 days unless, broadly, members have passed a resolution to allow 14 days' notice at the preceding AGM or a general meeting held since the AGM. Companies may wish to do this before 3 August 2009 to be able to continue to hold meetings at 14 days' notice between that date and their next AGM. The government has issued guidance – see [www.berr.gov.uk/whatwedo/businesslaw/eu-company-law/directives/page49116.html](http://www.berr.gov.uk/whatwedo/businesslaw/eu-company-law/directives/page49116.html). For a more detailed discussion of these points, see Parts 3 and 4 of this guide.

For UK companies, many of the Directive's provisions should not cause problems because they broadly follow the approach normally adopted in the UK and some of the Directive's provisions have already been implemented by the 2006 Act. There will be a bigger effect in member states where it is more difficult for shareholders to access information about meetings and to participate in general meetings and exercise their rights as shareholders, particularly if they cannot attend the meeting in person. The Directive should make it much easier to do this across the EU. However, some of the provisions in the Draft Regulations will cause problems for companies (and are not required by the Directive). Companies will also want to decide what approach to adopt to amending their articles at their 2009 AGMs.

### **Proposed changes to the 2006 Act**

As well as implementing the Directive, the Draft Regulations change some of the shareholders' rights provisions in the 2006 Act. In these cases the proposed changes will apply to all companies, whether traded or not. These are discussed in Parts 3 and 4 of this guide.

## Part 2 – Financial reporting

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### Timeline

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Year beginning on or after 1 October 2007	Business review – scope of reporting requirements expanded.
Year beginning on or after 6 April 2008	2006 Act's accounts and audit provisions in force – changes in political donations disclosures, publishing accounts on website.
Year beginning on or after 29 June 2008	Amendments to Combined Code – committee membership, multiple chairmanships.
	Changes to wording of Listing Rules 'comply or explain' statement.
	New Financial Services Authority (FSA) corporate governance statement.
	Audit committees – new FSA disclosure requirements.
1 October 2008 onwards	Reporting on directors' conflicts procedures.
Year beginning on or after 6 April 2009	New directors' remuneration report rules – taking into account other employees' pay and conditions.
Year ending on or after 30 June 2009	Audit committee – changes to Smith best practice guidance (see below) – audit selection disclosures.
1 October 2009	Deadline for government guidance on measuring and calculating greenhouse gas emissions.
6 April 2012	Deadline for regulations requiring emissions reporting.

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### Expanded business review under the 2006 Act

For financial years beginning on or after 1 October 2007, the business review of a quoted company must include, to the extent necessary for an understanding of the development, performance or position of the company's business:

- the main trends and factors likely to affect the future development, performance and position of the company's business;
- information about environmental matters, the company's employees and social and community issues (including information about the company's policies on these issues and their effectiveness); and
- information about persons with whom the company has contractual or other arrangements essential to its business (unless disclosure would, in the directors' opinion, seriously prejudice that person and be contrary to the public interest).

In the parliamentary debates on the 2006 Act, the government stated that companies would not be required to list their suppliers and customers, or to provide detail about contracts, but they would have to report significant relationships likely to influence, directly or indirectly, the business's performance and value. It gave some examples:

'Where a company provides the vast majority of its products or services to one customer, the arrangements might well be essential and therefore disclosable, particularly if the company could not be sure of finding an alternative buyer for its product. Similarly, where a company relies on a single supplier for a key component, so that, if that supplier went bust, that would have a serious impact on the company's business, then that too would be disclosable. But where a company is buying products or services from a number of suppliers, or could switch suppliers, then it is much less likely that it would be necessary to disclose details of a particular supplier to give an understanding of the development, performance or position of the business. Similarly, if a company has a wide market of customers, then the directors might judge it unnecessary to disclose information about any particular customer.'

Companies are exempted from disclosing information about impending developments or matters in the course of negotiation if, in the directors' opinion, disclosure would be seriously prejudicial to the company's interests.

The Accounting Standards Board (ASB) has reminded companies that these requirements are already included in its *Reporting statement on operating and financial review* issued in January 2006. In the ASB's view, the OFR reporting statement continues to provide applicable best practice guidance for all UK companies that are required to prepare a business review. To help UK companies in preparing their business reviews, the ASB has produced a table showing where the requirements of the 2006 Act are reflected in the OFR reporting statement – [www.frc.org.uk/asb/press/pub1480.html](http://www.frc.org.uk/asb/press/pub1480.html).

In its statement of priorities for 2008-2009, the Financial Reporting Review Panel (FRRP) focused in particular on disclosures relating to financing arrangements and uncertainties in the light of credit market conditions at the time of approval of financial statements. For 2009-2010 it has said that it will review the adequacy of the disclosures required to be included in the

business review in terms of ‘what a reasonable board might be expected to conclude on the basis of information available when the accounts are approved’. The FRRP expects to see, where appropriate, an account of how the directors are managing the risks that the company faces.

### **Reporting on going concern in current financial climate**

The Listing Rules require the annual reports of listed companies to include a statement by the directors that the business is a going concern, with supporting assumptions or qualifications as necessary. The directors must consider Financial Reporting Council (FRC) guidance on going concern published in November 1994 (reprinted in November 2008; [www.frc.org.uk/publications/pub1775.html](http://www.frc.org.uk/publications/pub1775.html)).

The FRC has been consulting on whether the existing guidance can be improved in the light of deteriorating economic conditions. Its approach is that the 1994 guidance should be retained with minimum amendment, but stakeholders have been asked whether more fundamental changes are necessary. The consultation document is available at [www.frc.org.uk/images/uploaded/documents/Going%20concern%20draft%204%20vs1.pdf](http://www.frc.org.uk/images/uploaded/documents/Going%20concern%20draft%204%20vs1.pdf).

In the meantime, it has published an update on going concern and liquidity risk – [www.frc.org.uk/publications/pub1784.html](http://www.frc.org.uk/publications/pub1784.html). It does not create any new rules, but summarises existing requirements for listed companies’ going concern and liquidity risk disclosures in annual reports and accounts and comments on how they apply in the light of current financial conditions. For example, the update covers:

- the implications of a bank or other lender failing to confirm the continued availability of finance facilities; and
- the need to improve the clarity of information provided in annual reports about how liquidity risk is managed in practice – in particular, the FRC criticises the way the relevant information is often spread around the annual report, making it difficult for users to appreciate the full picture, and suggests ways of improving presentation.

The update also contains useful examples of going concern disclosure wording, including for companies that are having liquidity issues.

In December 2008 the Auditing Practices Board (APB) published Bulletin 2008/10 *Going concern issues during the current economic conditions* to help auditors respond to the challenge of current economic conditions, especially the uncertainty over:

- bank lending intentions and the availability of finance more generally;
- the recession’s effects on a company’s own business; and
- the recession’s effects on customers and suppliers.

One consequence is expected to be an increase in the disclosures in annual reports and accounts about going concern and liquidity risk. Auditors will

need to ensure that they fully consider going concern assessments and refer to going concern in their auditor's reports only when appropriate.

### **Reporting on directors' conflicts procedures**

The 2006 Act's provisions dealing with conflicts of interest came into force on 1 October 2008. The new rules are discussed in detail in our guides *Companies Act 2006: conflicts of interest – a guide for directors* and *Companies Act 2006: directors' conflicts – a guide for company secretaries*. These guides discuss, for example, the typical situations in which directors may need board authorisation under the 2006 Act, with a checklist of practical points for the board's authorisation decision. The Association of General Counsel and Company Secretaries of the FTSE 100 (GC100) has also published several notes and checklists providing guidance on the new rules. These are available at [www.practicallaw.com/2-200-3996](http://www.practicallaw.com/2-200-3996).

The GC100 has suggested that the board should consider how it could give shareholders assurance that its authorisation powers are being exercised properly and in accordance with the articles – for example, by means of an explanation in the annual directors' report. The Association of British Insurers (ABI) has asked companies to follow emerging best practice in line with the GC100 guidance – in particular, the board should report annually that it has procedures to deal with conflicts of interest and that they operate effectively. Many companies committed to reporting annually on procedures when they sought shareholder approval for conflicts-related changes to articles.

### **Takeovers Directive – disclosures about share capital**

The FRRP has reminded companies about the disclosure requirements for directors' reports arising under the EU Takeovers Directive – [www.frc.org.uk/frp/press/pub1522.html](http://www.frc.org.uk/frp/press/pub1522.html). It has found that some companies have not been complying fully with these requirements.

For financial years beginning on or after 20 May 2006, directors must provide the following information (with 'any necessary explanatory material') in their annual report and summary financial statement:

- the structure of the company's share capital;
- any restrictions on transfer of securities in the company;
- significant direct or indirect holdings;
- any shareholders with special control rights and the nature of these rights;
- if shares to which an employees' share scheme relates have rights with regard to control of the company not exercisable directly by employees, how those rights are exercisable;
- any restrictions on voting rights;
- any agreements between shareholders known to the company that may restrict transfers of securities or voting rights;

- the rules governing the appointment and replacement of board members and changes to the articles of association;
- the board's powers, including in particular over the issue or buy-back of shares;
- any significant agreements to which the company is a party that take effect, alter or terminate upon change of control of the company following a takeover bid; and
- any agreements providing for compensation to board members or employees resulting from resignation or redundancy or otherwise following a takeover bid.

The requirements apply to all companies registered in the UK that have voting securities admitted to trading on a regulated market within the EU or EEA. They apply whether or not the company is involved in a takeover.

For financial years beginning on or after 29 June 2008, this information must, under new FSA rules discussed further below (see 'New FSA corporate governance statement'), appear in the corporate governance report – previously they could appear anywhere in the directors' report. These disclosures may therefore have to be re-organised.

#### **Changes to the Combined Code and 'comply or explain' statement**

In 2007 the Financial Reporting Council (FRC) carried out a limited review of the effects and effectiveness of the 2006 Combined Code, concluding that it was working reasonably well with no need for major changes. But it emphasised that there was room for improvement in the way the Combined Code was applied by companies, investors and intermediaries.

A revised Combined Code has come into effect for financial years beginning on or after 29 June 2008. The key changes:

- remove the restriction on an individual chairing more than one FTSE 100 company;
- allow the chairman of a smaller listed company (ie those outside the FTSE 350) to be a member of the audit committee – but not its chair – if he or she was considered independent on appointment; and
- reflect changes to FSA rules in force from June 2008 (these are discussed in the next two sections below).

Requirements for reporting against the Combined Code have also changed. The Listing Rules now require a company to report on how it has applied the 'main principles' set out in section 1 of the Combined Code; previously, companies were required to report against all the elements of the supporting principles as well. Reflecting this change, the preamble to the Combined Code now states:

'In relation to the requirement to state how it has applied the Code's main principles, where a company has done so by complying with the associated

provisions it should be sufficient simply to report that this is the case; copying out the principles in the annual report adds to its length without adding to its value. But where a company has taken additional actions to apply the principles or otherwise improve its governance, it would be helpful to shareholders to describe these in the annual report.’

If a company chooses not to comply with the Combined Code, the board should give shareholders a ‘careful and clear explanation’ that aims to ‘illustrate how its practices are consistent with the principle to which the particular provision relates and contribute to good governance’. The board will need to review the explanation in its corporate governance statement to ensure that this objective is achieved, because the 2006 edition recommended simply that companies ‘review each provision carefully and give a considered explanation if it departs from the Code provisions’.

The revised preamble emphasises that the Combined Code is not a rigid set of rules and that disclosures should give shareholders ‘a clear and comprehensive picture of a company’s governance arrangements’. Boards may wish to review the content of their corporate governance reports to see if there is any scope for providing more specific information that more closely reflects the particular circumstances of the company and the practices of the board.

The Combined Code’s revised preamble also places more emphasis on the need for improved engagement on governance issues by shareholders (or their agents) with the board, particularly if a company has departed from the Combined Code. Shareholders are encouraged to evaluate carefully the explanations given by boards and to discuss their views, rather than automatically treating departures as a ‘breach’.

### **New FSA corporate governance statement**

The FSA has added a new chapter to its Disclosure and Transparency Rules (DTRs) to implement parts of the EU Statutory Audit Directive and Company Reporting Directive.

For financial years beginning on or after 29 June 2008, companies must publish a corporate governance statement in the annual directors’ report (or in a separate statement published with, and in the same way as, the directors’ report) that includes, broadly:

- a reference to the national corporate governance code that the company applies or is subject to;
- a statement of where the relevant corporate governance code is publicly available;
- to the extent that the company departs from that code, an explanation of which parts of the code it departs from and the reasons for doing so;
- a description of the company’s internal control and risk management systems ‘in relation to the financial reporting process’;

- information about the company's share and control structures; and
- details of the composition and operation of the board and its committees.

This should not have any substantial effect on companies that already comply with existing 'comply or explain' requirements in the FSA's Listing Rules (see the discussion above). The FSA has issued guidance that compliance with those provisions satisfies the DTRs' requirements.

The FRC has footnoted the Combined Code to highlight the areas of overlap between the Combined Code and the FSA rules and has emphasised that, although companies can choose to comply with the Combined Code or explain non-compliance, they are bound to comply with the DTRs' equivalent provisions.

The requirement that the corporate governance report should include a description of the main features of the company's internal control and risk management systems in relation to the financial reporting process is different from the Combined Code provision requiring the board to report that a review of the internal control system's effectiveness has been carried out. Boards should review their corporate governance reports to ensure that they are satisfied that sufficient information is provided to meet the DTRs' requirements.

#### **New FSA rules on audit committees**

The FSA has also made changes relating to audit committees. The EU Statutory Audit Directive requires companies with transferable securities admitted to trading on a regulated market in a member state to have an audit committee or an equivalent body that meets the Directive's requirements. This body should be responsible for:

- monitoring the financial reporting process;
- monitoring the effectiveness of the internal control, internal audit and risk management systems;
- monitoring the statutory audit; and
- reviewing and monitoring the independence of the external auditor and, in particular, the provision of additional services to the company.

These requirements are less onerous and detailed than the existing audit committee provisions of the Combined Code.

The FSA has amended the DTRs to require a company to have an audit committee with at least one independent member and a member who has competence in accounting and/or auditing – these may be the same person. The rules do not prescribe what would constitute independence or relevant financial expertise in this context. The government and FSA have said that these matters are 'appropriate to be judged ultimately in the individual circumstances of the company and in relation to the nature and complexity of the business'.

The company must issue an annual statement identifying the body carrying out audit functions and describing its composition. This disclosure may be made in the corporate governance report.

Any decision to appoint a statutory auditor must be based on a recommendation made by this audit body.

The FSA has issued guidance that:

- compliance with the Combined Code audit committee provisions will be sufficient to satisfy the DTRs' relevant requirements; and
- disclosures about the audit committee required by the DTRs could be included in the description of the audit committee's work currently required by the Combined Code.

For most companies, the audit committee already operates in a way that meets these FSA requirements.

#### **Updated Smith guidance for audit committees**

The FRC published updated *Guidance on audit committees* (known as 'the Smith guidance') in October 2008. It provides best practice guidance to boards on the audit committee provisions of the Combined Code and assists directors serving on audit committees.

The guidance requires more disclosure in annual reports about the process of auditor selection – in particular, boards should disclose any contractual obligations to appoint certain types of audit firms. It also prompts audit committees to consider the risks associated with their external auditor leaving the market and suggests factors to be considered if a group is considering engaging firms from more than one network to work on the audit.

The revisions to the guidance took immediate effect except for those on disclosure about audit selection, which will apply to financial years ending on or after 30 June 2009.

#### **Changes to statutory annual report requirements – auditors' liability limitation agreements, political donations and signing audit reports**

The 2006 Act provides a framework for annual reports, with the detailed requirements on form and content to be set out in regulations. These apply in most cases for financial years beginning on or after 6 April 2008.

The regulations largely restate existing rules, but there are some differences. For example:

- companies must disclose liability limitation agreements that they make with their auditors in a note to the company's annual accounts (liability limitation agreements are discussed in Part 4 of this guide);
- the thresholds for disclosure of political donations and expenditure and charitable donations have been raised from £200 to £2,000;

- the directors' report must disclose details of donations in excess of £2,000 to independent election candidates as well as other political donations (unless the company is a wholly owned subsidiary of a UK parent); and
- audit reports must be signed by and name the individual lead auditor, as well as the audit firm (although provision is made for confidentiality in exceptional cases).

BERR has published guidance on the accounting and reporting provisions introduced under the 2006 Act – [www.berr.gov.uk/files/file46791.pdf](http://www.berr.gov.uk/files/file46791.pdf). It outlines the substantive changes introduced by the 2006 Act and discusses their effects.

### **Price-sensitive information and annual results**

The FSA has reminded companies that they must disclose price-sensitive information about their financial positions as soon as possible – [www.fsa.gov.uk/pubs/ukla/list\\_feb08.pdf](http://www.fsa.gov.uk/pubs/ukla/list_feb08.pdf).

If a company discovers it holds price-sensitive information when it compiles its annual results, it may need to bring forward any pre-planned announcement date. In particular, the FSA emphasises that:

- if a company makes any announcements in the run-up to releasing its annual reports, or during their release, it should make them so that investors have the necessary information to make informed decisions;
- all formal and informal information that a company presents should give investors an understanding of the basis of the quantitative disclosures being made – eg information on valuation methods and assumptions, funding and liquidity; and
- disclosures in annual financial reports must give a fair review of the company's business and a description of the main risks and uncertainties it faces.

### **Model Code – FSA clarifies close periods for quarterly reporting**

The FSA has clarified that the Model Code close period for a company reporting quarterly financial information is the 30 days preceding the publication of the results for each of the first, second and third quarters and 60 days for the fourth quarter. There is no close period preceding the publication of an interim management statement.

For annual results, the close period is the 60 days before a company publishes either its preliminary statement or its annual financial report. For the half-year report, the close period runs from the end of the relevant financial period up to and including the time of publication.

### **Preliminary results announcements**

Preliminary results announcements are no longer mandatory for financial years beginning on or after 20 January 2007. The FSA has confirmed that, if a company chooses to make a preliminary results announcement, neither

the Listing Rules nor the DTRs require it to be prepared in accordance with IAS 34, but it must comply with Listing Rules requirements.

Under the Listing Rules, a company must agree the preliminary announcement with its auditor before publication. The APB has issued a bulletin reflecting the fact that preliminary announcements are now optional, giving guidance on:

- the procedures the auditor should normally carry out before agreeing a preliminary announcement;
- the implications of reaching agreement before the auditor's report on the full financial statements has been signed;
- matters to be dealt with in the audit engagement letter relating to a preliminary announcement; and
- the implications of a preliminary announcement, including alternative performance measures and management commentary.

#### **Publishing accounts – shorter deadlines and using websites**

The FSA has reminded companies that they must publish their annual reports and accounts within four months of their year-ends – publishing preliminary results within this period does not satisfy this requirement ([www.fsa.gov.uk/pubs/ukla/ukla\\_update.pdf](http://www.fsa.gov.uk/pubs/ukla/ukla_update.pdf)). The FSA has the power to suspend listing or take enforcement action if the deadline is missed.

The 2006 Act requires annual accounts and reports for financial years beginning on or after 6 April 2008 to be published on a website.

For non-US companies that have reporting obligations to the US Securities and Exchange Commission (SEC), the reporting deadline for annual reports filed on Form 20-F has been reduced from six months to four months after the company's fiscal year-end – see 'US developments' below for more information.

#### **FSA guidance on half-yearly report requirements**

##### **Describing risks and uncertainties**

Companies must include in the annual report and in the interim management report section of a half-yearly report a description of the principal risks and uncertainties that the company faces. The FSA gave some guidance on this in issue 18 of its newsletter *List!* (available at [www.fsa.gov.uk/pubs/ukla/list\\_mar08.pdf](http://www.fsa.gov.uk/pubs/ukla/list_mar08.pdf)). If the principal risks and uncertainties set out in a company's annual report remain valid for the purpose of the interim management report, it is acceptable for the half-yearly report to:

- state that the principal risks and uncertainties have not changed;
- provide a summary of those principal risks and uncertainties; and
- include a cross-reference to the detailed explanation of them, giving its location in the annual report.

The FSA encourages companies to consider the effect of the current economic turbulence in the credit environment when deciding whether to include any additional description of principal risks and uncertainties in the half-yearly report.

#### **Responsibility statements**

Annual and half-yearly reports must include a responsibility statement. The FSA explained in *List!* 18 that in most cases it expects either the whole board of directors, or one or more directors on behalf of the whole board, to be named as responsible for the half-yearly report. The name and function of those responsible should be stated in the responsibility statement itself – it is not sufficient to cross refer to other documents.

#### **Announcing the half-yearly report on a RIS**

The FSA's rules on disseminating regulated information require issuers to disclose the half-yearly report (which falls within the definition of 'regulated information') to the public through a regulatory information service (RIS). The regulated information must be communicated to the media in unedited full text.

The FSA has criticised the practice of including half-yearly report information on a company's website when it has not been included in the RIS announcement. It has stressed that all the items that the DTRs require to be included in the half-yearly report should be in the RIS announcement.

#### **Legal liability for accuracy of reports**

There has been concern in recent years that increased periodic financial reporting requirements may increase the legal liability of a listed company and its directors and auditors for the accuracy of financial reports. It has been argued that liability may extend beyond existing shareholders to all potential investors and may also arise under the laws of each of the 27 member states.

#### **Protecting companies**

To help protect companies against this possible extended liability, at least in the UK, the 2006 Act set up a statutory liability regime. Under this law, a company is liable to compensate an investor who has acquired securities and suffered a loss as a result of an untrue or misleading statement in, or omission from, an annual, half-yearly or interim management report, or a preliminary statement of annual results. But to be liable it must be shown that a director knew or was reckless as to whether the statement was wrong or misleading, or must have known that any omission was a dishonest concealment. Only the company is liable to the investor, although the director concerned may be liable to the company.

Following a formal review conducted at the Treasury's request, Professor Paul Davies published a report making the case for extending the statutory liability regime set up by the 2006 Act for regular financial reports required by the DTRs. In July 2008 the Treasury published a consultation paper setting out the government's proposals on extending the statutory regime,

using a power provided by the 2006 Act – in particular, to cover a broad range of ad hoc and periodic disclosures to markets. The consultation paper is available at [www.hm-treasury.gov.uk/d/issuerliability\\_170708.pdf](http://www.hm-treasury.gov.uk/d/issuerliability_170708.pdf).

#### **Protecting directors**

The 2006 Act introduced a safe harbour restricting directors' civil liability for the content of directors' reports and directors' remuneration reports (and summaries of those reports). The safe harbour applies to reports and statements first sent to members on or after 20 January 2007. Broadly:

- a director is liable to the company for any loss it suffers as a result of
  - (1) any untrue or misleading statement in a report, if the director knew or was reckless as to whether the statement was untrue or misleading; or
  - (2) any omission from a report of anything required to be included in it that the director knew to be a dishonest concealment of a material fact;and
- a director is not liable to any other person (eg a shareholder or a potential investor in the company) in respect of the contents of those reports or summaries. This does not affect any potential criminal liability relating to the reports or any civil penalty.

The safe harbour does not apply to statements made in related documents, such as a chairman's letter sent to shareholders with the report and AGM notice.

#### **Looking forward – reporting on directors' remuneration**

For financial years beginning on or after 6 April 2009, the directors' remuneration report must contain a statement on how the pay and employment conditions of employees of the company and other undertakings in the company's group have been taken into account when determining directors' remuneration for the relevant financial year. For more information about the directors' remuneration report please refer to our guide *Directors' Remuneration Report Regulations: checklist, commentary and related best practice*, which is available at [www.freshfields.com](http://www.freshfields.com).

In December 2008, Lord Gavron introduced a private member's bill that would require quoted companies to 'publish on the first page of the chairman's statement, chief executive's statement or directors' report, whichever comes first in the annual accounts and report, the ratio between the total annual remuneration of the highest paid director or executive and the total annual average remuneration of the lowest paid ten per cent of the workforce'. This is unlikely to become law.

#### **Looking forward – climate change reporting**

The Climate Change Act, which received Royal Assent at the end of November 2008, requires the Secretary of State to:

- make regulations under the 2006 Act requiring directors' reports to contain certain specified information about emissions of greenhouse gases from activities for which the company is responsible, or lay a report

before parliament explaining why no such regulations have been made, not later than 6 April 2012; and

- publish guidance not later than 1 October 2009 on the measurement or calculation of greenhouse gas emissions to assist people in reporting on such emissions from activities for which they are responsible.

The government will consult in 2009 on defining and measuring companies' carbon emissions and has said that the outcome of that consultation will be reflected in the guidance.

### **Looking forward – reporting on equal pay**

It has been reported that the government is drawing up an amendment to the Equality Bill that would require companies to publish figures in annual reports showing the number of male and female employees in particular pay bands. The bill – to replace the Equal Pay Act 1970 – is due to be published in the next few months.

### **US developments**

#### **Non-US company exemption from inadvertent Exchange Act registration**

The US Securities Exchange Act of 1934 provides an exemption from the Exchange Act registration requirement that is otherwise triggered when some non-US companies exceed certain shareholder and asset thresholds.

Previously, companies claimed the exemption by submitting a paper application and sending paper copies of their home-country disclosure to the SEC regularly afterwards.

As a result of amendments in 2008 – <http://sec.gov/rules/final/2008/34-58465.pdf> – the exemption applies automatically (without application to the SEC and without regard to the number of US shareholders) to non-US companies that meet three conditions:

- non-SEC reporting – the company must not already be required to report to the SEC under the Exchange Act;
- home-country listing – the securities in question must be listed on one or more non-US exchanges that constitute the company's 'primary trading market' (ie at least 55 per cent of these securities are traded in one or no more than two non-US jurisdictions). If trading in two jurisdictions is aggregated to constitute a primary trading market, then trading in at least one of those jurisdictions must be at a higher volume than in the US; and
- electronic publication of home-country disclosure – the company must have published its home-country disclosure documents electronically and in English, for example on its website, and the documents must have been published from the first day of the company's most recent fiscal year. Documents include: (a) information made public in the company's home jurisdiction, (b) information filed with the principal stock exchange in the primary trading market and which has been made public by that exchange and (c) information distributed to security holders.

Companies that already use the exemption are no longer allowed to submit paper copies of their home-country disclosures to maintain the exemption. To continue to retain the exemption, they must meet and continue to meet the conditions. There is a three-year transition period to allow time for companies already using the exemption either to meet the conditions or register under the Exchange Act. Companies using the exemption that cease in future to meet the conditions will lose the exemption and must then register.

The amended rule aims to facilitate access for US investors to non-US companies' material home-country disclosure documents and to foster increased trading of non-US companies' securities in the US over-the-counter market. (The exemption enables a non-US company to have its equity securities traded on a limited basis in the US over-the-counter market without SEC registration.)

#### **Interpretive guidance on use of company websites**

The SEC has issued updated guidance on how companies can use their websites to provide information to investors in compliance with the US federal securities laws – [www.sec.gov/rules/interp/2008/34-58288.pdf](http://www.sec.gov/rules/interp/2008/34-58288.pdf). This is helpful with the increasing use of electronic disclosure by non-US companies – as shown by new requirement to provide home-country disclosure electronically discussed above.

The new guidance relates to antifraud liability under the US federal securities laws if information has been disclosed electronically. The extraterritorial reach of the US federal securities laws means that a non-US company can potentially incur antifraud liability for activities that take place outside the US if it is reasonable to expect those activities to have an effect within the US (regardless of whether the company is an SEC-reporting company).

Generally, statements made by a company on the internet are treated in the same way as any other statement made by or attributable to the company for antifraud purposes.

Topics covered by the new guidance on antifraud liability include:

- previously posted materials on company websites – the SEC stated that previously posted information on a company's website is not considered re-issued or republished for antifraud purposes just because it is accessible, as long as it is apparent to a reasonable person that the information is historical by being clearly identified as such and located in a separate section on the website containing previously posted information;
- hyperlinks to third party information – in 2000, the SEC stated that whether a company is liable for third party information for which it provided a hyperlink depended on whether the company was involved in preparing the information and explicitly or implicitly endorsed the information. The SEC's new guidance states that the company should

also explain the context for the hyperlink and attempt to reduce the risk of confusing investors – for example, by including cautionary language. A company cannot shield itself from liability through the use of disclaimers if it knew or was reckless in not knowing that the linked information was materially false or misleading; and

- summary information – when using summaries or overviews on websites, companies should make it clear to readers that the information is a summary and direct them to the location of the detailed disclosure from which the summary is derived.

#### **Interactive data for financial reporting**

Non-US companies that report to the SEC are to be required to file their financial statements in an interactive data format using eXtensible Business Reporting Language (XBRL) – see [www.sec.gov/news/speech/2008/spch121708mwwg.htm](http://www.sec.gov/news/speech/2008/spch121708mwwg.htm). The requirement will be phased in over three years from 15 June 2009. It applies to non-US companies whether they prepare their financial statements under US GAAP or IFRS and to US companies that report to the SEC.

#### **Non-US company reporting enhancements**

Non-US companies that have SEC reporting obligations are subject to amendments to various rules adopted by the SEC in December 2008 (Foreign Issuer Reporting Enhancements or FIRE) – <http://sec.gov/rules/final/2008/33-8959.pdf>.

In brief, the FIRE amendments include:

- accelerating the reporting deadline for annual reports filed on Form 20-F from six months to four months after the issuer's fiscal year-end, following a three-year transition period;
- allowing a non-US company to assess its eligibility as a 'foreign private issuer' on an annual basis on the last business day of its second fiscal quarter, rather than on a continuous basis as previously required;
- requiring a reconciliation to US GAAP in annual reports and registration statements under item 18 of Form 20-F (financial statements) and eliminating the availability of limited US GAAP reconciliation under item 17 of Form 20-F, with effect from 15 December 2011. This change applies only to non-US companies that remain subject to the reconciliation requirement because they do not file financial statements prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB);
- eliminating the option to omit segment data disclosure from US GAAP financial statements, with effect from the first fiscal year ending on or after 15 December 2009;

- requiring disclosure in annual reports filed on Form 20-F of any change in the company's certifying accountant, with effect from the first fiscal year ending on or after 15 December 2009;
- requiring annual disclosure of fees and other charges paid by holders of American depositary receipts (ADRs) to depositaries, as well as any other charges paid by depositaries to the company whose securities underlie the ADRs, with effect from the first fiscal year ending on or after 15 December 2008; and
- requiring disclosure in annual reports filed on Form 20-F by a listed non-US company of any significant differences between its corporate governance practices and those applicable to US companies under the relevant exchange's listing standards, with effect from the first fiscal year ending on or after 15 December 2008. This change reflects disclosure already required of non-US companies by the US exchanges on which they are listed (on the website or in the annual report) but mandates its inclusion in the annual report.

## Part 3 – The business of the 2009 AGM

### Headlines for 2009

- Articles – what changes are advisable to implement the 2006 Act?
- Articles – what changes are advisable to implement the Directive?
- Should the articles be altered in 2009 or later?
- Abolishing the objects clauses and authorised share capital – what does the company need to do?
- Share allotment authorities – implementing the new ABI and Pre-Emption Group guidance.
- Allowing 14 days' notice of general meetings – new annual AGM resolution requirements.
- Political donations – does the company need to amend the AGM notice?
- Auditors' limitation of liability agreements – the new rules.

### Introduction

In this part of the guide we discuss how the 2006 Act and the Draft Regulations may affect the scope of the business to be dealt with at companies' 2009 AGMs. For most companies, the 2006 Act does not require any change to many of the resolutions that are routinely put to shareholders at the AGM. Even when the 2006 Act is fully in force, we do not expect to see any change to the wording of typical resolutions on reports and accounts, directors' re-appointments and dividends.

### Articles – what changes may be necessary under the 2006 Act?

#### Introduction

At their 2008 AGMs, many companies asked shareholders to make changes to the articles to reflect all or part of the 2006 Act. In some cases two resolutions were put to the AGM: the first adopting new articles immediately (to reflect the parts of the 2006 Act already in force – eg the new rules on electronic communications with shareholders) and the second to adopt new articles with effect from 1 October 2008 (to reflect 2006 Act provisions coming into force on that date – eg the new rules on directors' conflicts of interest). In a small number of cases companies asked shareholders to adopt three versions of the articles, coming into force on the passing of the resolution at the 2008 AGM, on 1 October 2008 and on 1 October 2009 respectively.

Whether or not they have made any changes to their articles over recent years, companies should now consider whether to ask shareholders to amend them to take account of the final implementation of the 2006 Act on 1 October 2009. We discuss the main changes they need to think about in the following paragraphs. Many companies will already have made some of these changes.

### Key changes – 2006 Act provisions coming into force October 2009

#### Memorandum of association

The Companies Act 1985 (the 1985 Act) requires a company to state its objects in the memorandum. Under the 2006 Act, companies incorporated

on or after 1 October 2009 will have unlimited objects unless restrictions are set out in the articles.

The objects clauses of an existing company's memorandum will be treated as provisions of its articles from 1 October 2009. The Order provides that the company may comply with any obligation to send a person a copy of its articles by either appending a copy of the provisions of its old-style memorandum that are deemed to be provisions of the articles to a copy of the other provisions of the articles or sending a copy of its old-style memorandum with a copy of the other provisions of the articles.

Companies should decide whether to ask shareholders to approve the deletion of relevant parts of the memorandum from the articles with effect from 1 October 2009. We expect most companies will do this at their AGMs in 2009.

#### **Share capital – authorised share capital**

The 2006 Act abolishes the requirement to have authorised share capital with effect from 1 October 2009. The Order contains transitional provisions for existing companies – public and private:

- from that date, any provision in a company's memorandum of association on the amount of the authorised share capital (as amended under the 1985 Act) will be treated as a provision in the articles setting the maximum amount of shares that the company may allot;
- the company may amend or revoke this provision by ordinary resolution – if the resolution is passed before 1 October 2009 it is treated as passed on that date; and
- an amendment of a company's articles on or after 1 October 2009 to authorise the directors to allot shares in excess of the maximum amount set out in the memorandum will be effective even though it does not expressly amend or revoke the provision.

This does not affect the company's power to adopt new articles, with effect from 1 October 2009 or after, that make no provision on the maximum number of shares the company can allot.

We expect that many companies will ask shareholders to pass an ordinary resolution at the next AGM that will have the effect of removing the cap on allotment caused by the capital clause in the memorandum with effect from 1 October 2009. Companies will also have to look carefully at any references to share capital in their articles and remove them where appropriate. Institutional shareholders have yet to express their views, although we would not expect them to object because shareholder approval will still be needed to authorise directors to allot shares. In most cases it would also be sensible for private group companies to pass an ordinary resolution to give maximum flexibility in dealing with share issues.

#### **Share capital – other provisions**

Under the 1985 Act a company must have specific provisions in its articles enabling it to purchase its own shares, consolidate or sub-divide its shares and reduce its share capital or other undistributable reserves if it wants to do these things, as well as shareholder authority to undertake the relevant action. Existing articles usually include these enabling provisions. With effect from 1 October 2009 a company will require only shareholder authority to do any of these things and it will no longer be necessary for articles to contain enabling provisions. A company's articles may, however, contain prohibitions on these things.

The Order provides that shareholder resolutions authorising a buy-back that have been passed under the 1985 Act will remain effective after 1 October 2009.

The 2006 Act's provisions on redeemable shares make some substantive changes to the ways in which companies may issue redeemable shares and redeem them with effect from 1 October 2009. In particular, a private company will no longer need to have an authority in its articles before it may allot redeemable shares. The law will not change for public companies – they will have to be authorised by their articles before they can issue redeemable shares. Directors would need shareholders' authority to issue new shares in the usual way.

It will be possible for articles to give directors the power to determine the terms, conditions and manner of redemption of shares, rather than their being set out in the articles. Institutional investor groups have not yet expressed any views on this.

#### **Company names**

With effect from 1 October 2009, the 2006 Act allows the company's articles to permit its name to be changed other than by a shareholders' resolution. Companies may want to consider whether to ask shareholders to amend the articles to give this power to the board.

#### **Conforming the articles with the model articles**

The Companies (Model Articles) Regulations 2008 prescribe model articles for private companies limited by shares, private companies limited by guarantee and for public companies. They will apply instead of Table A to new companies formed on or after 1 October 2009 that do not register articles of their own with the registrar of companies. Companies incorporated before 1 October 2009 are not affected by the model articles but may choose to conform the language of some provisions of their articles to the model articles if they think it appropriate – for example, the provisions dealing with the automatic removal of directors in limited circumstances.

#### **Key changes – 2006 Act provisions already in force**

If a company has not already changed its articles to reflect these points, it may now wish to do so.

#### **Communications with shareholders and others**

The 2006 Act regime for communications between companies, shareholders, holders of debt securities and others came into force on 20 January 2007. This regime applies to any information or document required or authorised to be sent or supplied under the Companies Acts. This means it covers, but is not limited to, annual accounts and reports and notices of general meetings. Listed companies must also comply with FSA rules on electronic communications derived from the Transparency Directive.

The three basic types of permitted communication are hard copy, electronic communication (such as email or fax) and website publication. However, the rules do not require shareholders' express agreement to receive documents and information by website if certain conditions are met and procedures followed. As a result, website publication has become the default position for many companies, although shareholders can always obtain hard copies of documents free of charge if they wish. Companies still need a shareholder's express agreement to use email communication.

We discussed the statutory and FSA rules as they apply in the context of communications sent by a company to its shareholders in more detail in our guide *The 2008 annual report and AGM – hot topics*, which is available at [www.freshfields.com](http://www.freshfields.com). The Institute of Chartered Secretaries and Administrators (ICSA) published revised guidance on electronic communications with shareholders in March 2007, replacing its 2000 guidance.

In 2007 and 2008 many companies altered their articles to permit deemed agreement to website publication. Although it is possible to use this procedure without altering the articles if the shareholders pass a resolution to this effect, many companies chose to amend their articles to ensure consistency.

Even if they are already operating the new system, companies are likely to want to make sure the relevant authorisation to use website publication covers all documents and information required or authorised to be sent by the company – and not only those sent under the 2006 Act. It seems sensible to apply the same requirements to all documents and information. For example, the Takeover Code will be amended with effect from 30 March 2009 to enable offerors and offeree companies to use electronic forms of communication – including a website – to send information about offers to offeree company shareholders and others.

#### **Information rights**

The 2006 Act allows a nominee shareholder in a traded company – ie a company whose securities are admitted to trading on a regulated market – to nominate a person who holds a beneficial interest in a share to enjoy 'information rights'. Companies had to apply these rights from 1 January 2008.

Companies do not need to change the articles to enable a nominee to exercise his or her right to nominate a person to enjoy information rights, but it would be advisable to review the articles from this perspective to ensure they are consistent with the 2006 Act.

We discussed the new rules in detail in our guide *The 2008 annual report and AGM – hot topics*, which is available at [www.freshfields.com](http://www.freshfields.com). The ICSA has also published guidance on the information rights regime.

#### **Notice of general meeting**

The notice period under the 2006 Act for a general meeting other than an AGM is 14 clear days, even if a special resolution is proposed. This applies to public and private companies. Notice for a public company's AGM continues to be 21 clear days. The 1985 Act required a minimum of 21 days' notice for a special resolution, so articles may still be inconsistent with the 2006 Act provisions – and companies will have to give the longer notice period – until the articles are amended. The Combined Code continues to require at least 20 business days' notice for an AGM.

The Draft Regulations do not change the existing rules that require a minimum of 21 days' notice to call an AGM. But they will increase the notice required for other general meetings to 21 days even if only ordinary resolutions are being proposed. Fourteen days' notice will, however, be allowed (provided the company's articles also permit 14 days' notice) if members have passed a resolution approving shorter notice at the immediately preceding AGM or a general meeting held since the AGM. The company must also offer the facility for members to vote by electronic means accessible to all members who hold shares that carry rights to vote at general meetings.

This is explained more fully in 'Permitting short notice for general meetings' below.

#### **Proxies and corporate representatives**

Articles should reflect the increased proxy rights provided by the 2006 Act, which came into force on 1 October 2007. For example, shareholders should have the right to appoint more than one proxy for a meeting. The 2006 Act also allows proxies to vote – on a show of hands and on a poll – and speak at meetings. Although these rights apply notwithstanding anything in the company's articles, it prevents confusion if the articles are consistent with statutory requirements. Articles can only extend proxies' statutory rights, not reduce them.

The 2006 Act did not change the 1985 Act provision that any article that requires a proxy appointment to be received (or cancelled) by the company more than 48 hours before the time of the meeting is void, but the company may choose not to count weekends, Christmas Day, Good Friday and bank holidays. This means that if a meeting is to be held at, say, 11am on a Tuesday after a bank holiday Monday, the deadline for proxy submission cannot be earlier than 11am the previous Thursday. But the 2006 Act does

not prevent a company from setting a later deadline if the company's articles allow. Most companies that have not already done so will want to add a provision to their articles allowing the board full flexibility to choose any deadline that complies with statutory requirements, even if they do not propose to use it for the time being.

The 2006 Act provides that, if a corporate shareholder appoints more than one representative and they exercise the same power (such as voting) in different ways, the power is treated as not being exercised. A corporate shareholder can appoint more than one proxy – who can vote in different ways – but proxies must be appointed not less than 48 hours before the meeting, which can lead to difficulties in contentious situations or if a proxy appointment has not arrived before the deadline.

Institutional investor groups have expressed concern and the government has proposed alterations to this provision with effect from 3 August 2009. In due course companies will want to amend their articles to reflect these changes but in practice may not be able to do so at their 2009 AGMs. Until the changes come into force, investors are looking to companies to follow the best practice guidance issued by ICSA on dealing with multiple corporate representatives at general meetings and information to be given to shareholders. The guidance is available at [www.icsa.org.uk](http://www.icsa.org.uk). In particular, the ABI endorsed the ICSA guidance in its December 2008 *Articles of association and associated guidance* ([www.ivia.co.uk/ArticlesOfAssociation.aspx](http://www.ivia.co.uk/ArticlesOfAssociation.aspx)) and asked companies to disclose in the notes to their AGM notices that they would follow the ICSA guidelines.

#### **Directors' conflicts of interest**

The 2006 Act sets out the general duties owed by directors to their companies in a statutory code. Those on conflicts came into force on 1 October 2008. Many companies are now adopting more formal procedures for directors who have potentially conflicting interests, including if they hold multiple directorships.

The new rules are discussed in detail in our guides. For more information, see *Companies Act: conflicts of interest – a guide for directors* and *Companies Act: directors' conflicts – a guide for company secretaries*. The GC100 has also published papers and checklists on directors' conflicts of interest, containing guidance for directors on exercising the power to authorise conflicts, available at [www.practicallaw.com/6-378-7923](http://www.practicallaw.com/6-378-7923).

Some changes to articles are desirable. Companies that have not already done so should review the articles and make any amendments necessary to ensure they reflect the statutory regime and take advantage of permitted flexibility and protections. Importantly, directors of public companies can authorise a conflict only if the company's articles allow it – this requires express provision in the articles. Many public companies have made changes to their articles to include such provisions. The directors of private companies incorporated on or after 1 October 2008 are assumed to have

such powers unless the articles provide otherwise, but private companies incorporated before that date need to resolve to adopt this approach.

A provision in the 2006 Act allows companies to deal with conflicts of interest in their articles and provides that anything done in accordance with such a provision is not a breach of duty. We think it is helpful for the articles to contain provisions dealing with the use of confidential information received other than as a director of the company and provisions allowing a director to be absent from meetings or discussions if there is a conflict of interest.

## **Articles – changes required by the Draft Regulations**

### **Introduction**

As well as implementing the Directive, the Draft Regulations change some of the shareholders' rights provisions in the 2006 Act. In these cases the proposed changes will apply to all companies, whether traded or not.

We do not know what the final form of these changes will be; we expect them to differ significantly from the government's proposals. Because the government is not proposing to publish a summary of responses to its consultation paper until the end of April 2009, many companies will have to decide the approach to adopt for their 2009 AGMs before the Draft Regulations are finalised.

### **Corporate representatives**

As mentioned in 'Proxies and corporate representatives' above, if multiple representatives are appointed by corporate nominees to represent different beneficial owners wanting to vote in different ways, the 2006 Act has been interpreted as preventing the representatives from voting in different ways unless they are appointed as proxies (for which notice must be given to the company in advance). The 2006 Act will be amended to permit corporate representatives to vote in different ways from one another in respect of different blocks of shares.

### **Proxies' rights**

The Draft Regulations propose changes to the 2006 Act to clarify the rules that apply when a shareholder's proxy casts votes for different shares in different ways. On a show of hands, a proxy appointed by one member will have one vote and a proxy appointed by more than one member will have one vote if instructed to vote in the same way by all those members. If instructed to vote in different ways, the proxy will have one vote for and one vote against. If a shareholder has appointed more than one proxy, all the proxies taken together will have one vote or one vote for and one against. This means companies will still face practical difficulties if a nominee holding for different beneficial owners has appointed two or more proxies. The final version of the Draft Regulations may differ from the consultation version and companies are therefore not likely to want to make changes until the final position is clear.

### **Advance voting on a poll**

The Draft Regulations will allow shareholders to vote by correspondence – electronic or by post – if the company’s articles allow. Members can already appoint proxies electronically and by post, but the Directive requires member states to allow companies to give shareholders the option to vote directly in advance without appointing a proxy. Under current rules, a vote can be cast by proxy only if the proxy holder is present at the meeting to cast it.

The Draft Regulations will permit a company’s articles to contain a provision to the effect that, for a vote on a resolution on a poll taken at a meeting, the votes may include votes cast in advance. The government has asked for views on whether the right to demand a poll should also be exercisable in advance. Arguably, the Draft Regulations should also allow votes to be cast in advance if they are taken on a show of hands. A traded company is subject to the extra requirement that it can impose conditions to exercising this right only if they are necessary to ensure the person voting is identified – and the conditions must be proportionate to achieving that objective.

If a company includes this type of provision in its articles, it will not be able to require the advance vote to be registered, broadly, more than 48 hours before the time for holding the meeting (ignoring working days).

It seems unlikely that many companies will want to take advantage of this option in practice.

### **Proxies’ obligations**

The Draft Regulations create a new statutory obligation on a proxy to act in accordance with any instructions given by the member appointing him or her. We would not expect this to be reflected in the articles. It is arguable whether the new obligation is needed, because the general law probably already requires the proxy to vote in accordance with instructions. However, the Draft Regulations do not make it clear that the result of a vote is not affected if a proxy votes other than in accordance with their instructions. As companies have no way of knowing whether a proxy is following instructions, we hope the final version of the Regulations will make this clear and clarify a shareholder’s remedy if the proxy does not follow instructions.

## **Articles – complying with ABI guidance**

### **Introduction**

The ABI has published new guidance on articles (‘a key element of corporate governance and consequently of considerable interest to investors’) and associated topics: see [www.ivis.co.uk/PDF/3.5\\_Articles\\_of\\_Association.pdf](http://www.ivis.co.uk/PDF/3.5_Articles_of_Association.pdf). Companies will want to take account of this in drafting their articles. The following paragraphs outline some of the topics covered by the guidance.

### **Borrowing powers**

The ABI says that all companies should include a limit on the level of borrowings of the company or group in their articles and comments as follows:

- the model formulation is normally based on a multiple of capital and reserves (as taken from a company's published report and accounts);
- a broad figure for the borrowing limit in the articles is twice capital and reserves, but there may be wide variation depending on the company and sector;
- goodwill and intangible assets may be included in capital and reserves, subject to the provisions of FRS 10 or the equivalent international reporting standard requirements;
- netting off cash may be acceptable, but shareholders should be consulted before any change is proposed;
- fixed limits to borrowing powers should be kept under review; and
- excluding pension scheme deficits or surpluses is unlikely to be the most appropriate way of treating the effects of their volatility under the accounting standard.

### **Dispute resolution**

The ABI is concerned about companies wanting to include dispute resolution provisions – for example, exclusive jurisdiction or arbitration provisions – in articles and advises careful consultation with shareholders in such cases. In its March 2008 letter on this issue, the ABI said that this type of provision should not be seen as standard and should not be bundled with other changes to the articles. Even if not bundled, shareholders will expect a 'full and cogent' explanation (specific to the company's situation) of why the change should be supported. The National Association of Pension Funds (NAPF) views this type of clause 'in the first instance as a material reduction in shareholder rights'. Investors will normally oppose the provision unless the board clearly demonstrates that its benefits outweigh the diminution in shareholder rights because of the company's specific and extenuating circumstances.

### **Non-disclosure after section 793 notice**

Penalties for non-disclosure of an interest following a notice by the company requiring information about interests in shares under section 793 of the 2006 Act should comply with FSA rules.

### **Changes to share allotment authorities**

Companies with a section 80 authority and section 95 disapplication power in their articles may also need to change these provisions to reflect the new ABI guidelines on share allotments – see 'Issuing shares – directors' authority and disapplying pre-emption rights' below.

### **When to change articles**

If the resolutions for the company's AGM must be settled before the final form of the Draft Regulations is available (expected in late spring or early summer 2009), a company has a number of options. The following questions may help.

- Have the articles been amended to reflect the 2006 Act provisions already in force? If not, companies should consider asking shareholders to make some of these changes with immediate effect – for example, to provide for a 14-day notice period for general meetings, to enable the directors to authorise directors' conflicts and to permit deemed agreement to website publication of company communications.
- Does the company wish to amend or remove the provisions of the company's memorandum that are deemed to be part of the articles with effect from 1 October 2009 – ie the limit on the amount of shares that the company may allot (derived from the authorised share capital) and the objects clauses? If so, it should pass a resolution to this effect at the 2009 AGM.
- How does the company wish to deal with the 2006 Act provisions that will come into force on 3 August 2009 and 1 October 2009? The company could do this:
  - in two stages – ie at the 2009 AGM (to reflect the 2006 Act changes coming into force on 1 October 2009) and at the 2010 AGM (to reflect the 2006 Act changes in force on 3 August 2009); or
  - once only – ie at the 2010 AGM (by which time all relevant 2006 Act changes will be in force).

Assuming the articles reflect the 2006 Act provisions already in force and the company passes a resolution dealing with its authorised share capital and objects clauses at its 2009 AGM, we think most companies will wait until 2010 and make all these changes together.

Making changes to the articles for the provisions of the 2006 Act that come into force on 3 August 2009 is not without risk until we know the final form of the Draft Regulations. Companies doing this will almost certainly have to ask shareholders to amend the articles again at a later AGM because we expect the final form to differ considerably from the draft.

Companies with AGMs in autumn 2009 are in a better position and may be able to make all outstanding changes simultaneously if the final form of the Draft Regulations is published by early summer.

### **Permitting short notice for general meetings**

The Draft Regulations do not change the existing rules that require a minimum of 21 days' notice to call an AGM. The 2006 Act allows a minimum of 14 days' notice for other general meetings – subject to the company's articles – but the Draft Regulations will increase this to 21 days even if only ordinary resolutions are being proposed. Fourteen days' notice will, however, be allowed if:

- the company offers the facility for members to vote by electronic means accessible to all members who hold shares that carry rights to vote at general meetings;
- members have passed a resolution approving shorter notice at the immediately preceding AGM or a general meeting held since the AGM; and
- that resolution was passed either on a show of hands with no vote against or on a poll by a majority of not less than two-thirds of the total voting rights of all the members of the company who voted in person or by proxy on the resolution.

The provisions apply only to general meetings of shareholders and not to class meetings.

The members' resolution permitting 14 days' notice can last only until the company's next AGM. Companies will need to propose a resolution at each AGM from 2009 onwards if they want to be able to call other general meetings on 14 days' notice.

The Draft Regulations apply from 3 August 2009. This means that unless a company has passed an appropriate resolution at its 2009 AGM it will have to call any general meetings on 21 days' notice unless it calls a general meeting to pass an appropriate resolution (which is not likely to be attractive).

This may be important when the company, for example:

- needs to hold a meeting to increase its share capital and authorise the directors to allot shares to raise new money, when a shorter timetable will allow the company to reduce the underwriting costs associated with the fund raising; or
- needs shareholder approval for a large acquisition or disposal when the shorter notice period means, in the case of an acquisition, that the company will be at less of a timing disadvantage compared with rival purchasers that do not need shareholder approval or, in the case of a disposal, that the company can receive the consideration for the sale more quickly.

The Draft Regulations will allow adjourned meetings to be held on shorter notice if the adjournment is for lack of a quorum and the company has to issue a second or subsequent notice of meeting, provided no new item is put on the agenda for the meeting and there are at least 10 days between the original meeting and the date of the adjourned meeting.

BERR issued guidance in December 2008 identifying steps that listed companies may wish to take before 3 August 2009 to continue holding meetings at 14 days' notice pending the outcome of its consultation on the Draft Regulations – [www.berr.gov.uk/whatwedo/businesslaw/eu-company-](http://www.berr.gov.uk/whatwedo/businesslaw/eu-company-)

law/directives/page49116.html. It recommends that listed companies should consider proposing a special resolution at their next AGMs.

Even if a resolution is passed, a company would need to meet the requirements for electronic voting under the Directive before it can call a general meeting on 14 days' notice. BERR is consulting on how companies can satisfy the requirement for an electronic voting facility.

The FSA has confirmed that a circular proposing a resolution for a shorter notice period will not be considered one with unusual features under the Listing Rules. This means the FSA will not need to approve the circular.

### **Issuing shares – directors' authority and disapplying pre-emption rights The 2006 Act provisions – in force 1 October 2009**

The 2006 Act does not change the substance of the 1985 Act's provisions on directors' authority to allot shares (section 80) and disapplication of pre-emption rights (sections 89 and 95) for public companies. The Order provides that 1985 Act authorisations and disapplications in force immediately before 1 October 2009 have effect on and after 1 October 2009 as if given under the 2006 Act.

In most cases, we expect that listed companies are likely to continue to seek shareholder approval of authorities using their current wording for meetings convened before October 2009 (as amended by the ABI's new allotment guidelines – see 'ABI – changes to allotment guidelines' below). When the authority comes to be renewed under its terms – most likely at the next AGM after 1 October 2009 – changes to the wording of the relevant resolutions will be required.

The position may be different if the company's articles contain a section 80 authority and section 95 disapplication power and it passes short forms of resolution setting the 'section 80 amount' and 'section 89 amount' each year. In this case, some additions to the resolutions' wording may be advisable if the company is asking shareholders to adopt new articles with effect from 1 October 2009.

The 2006 Act will permit directors of private companies to allot shares without authorisation on and after 1 October 2009 if the company has one class of share (unless the articles provide otherwise). The Order has transitional rules for existing private companies:

- the new power to allot without authorisation will apply to an existing private company only if the members have resolved that the directors should have that power. It does not matter when the resolution is passed; and
- provisions in the articles of an existing company that require directors to be authorised under section 80 of the 1985 Act will be treated as provisions prohibiting the directors from exercising the new power to allot without authorisation – but not if the articles actually authorise directors under section 80.

We expect that many private group companies with one class of shares will pass resolutions to permit the directors to allot shares without authorisation.

If an existing private company's articles exclude pre-emption rights – taking advantage of section 91 of the 1985 Act – immediately before 1 October 2009, the exclusion will continue to have effect from that date as if it were given under the 2006 Act.

#### **ABI – changes to allotment guidelines**

The ABI has issued revised guidelines on share allotments and model resolutions in response to an invitation by the Rights Issue Review Group in its November 2008 report – [www.ivis.co.uk/ShareholdersPreemptionRight.aspx](http://www.ivis.co.uk/ShareholdersPreemptionRight.aspx). These increase the scope for a company to launch a rights issue without needing approval at a general meeting, potentially shortening the timetable for a capital raising.

Under the new guidelines, the cap on the annual allotment authority under section 80 of the 1985 Act has been increased from one-third to two-thirds of issued share capital, but:

- the amount of any authority above one-third must be applied only to fully pre-emptive rights issues; and
- the additional authority can be valid for one year only.

If the additional authority is taken and:

- the aggregate actual usage of the authority exceeds one-third as regards nominal amount; and
- in the case of issue being in whole or part by way of a fully pre-emptive rights issue, monetary proceeds exceed one-third (or such lesser relevant proportion) of the pre-issue market capitalisation,

the ABI expects all directors wishing to remain in office to stand for re-election at the next AGM after the decision to make the issue.

We expect that many companies will want to take advantage of the new guidelines by altering the wording of the section 80 and section 95 resolutions at their 2009 AGMs. They may also need to ask shareholders to increase the company's authorised share capital. We expect the ABI to regard this as a corollary of the increase in the permitted section 80 cap so that companies will not need to consult the ABI on this separately. Companies with a section 80 authority and section 95 power in their articles may need to change these provisions to reflect the new guidelines.

#### **Updated Pre-Emption Group statement of principles**

In its republished *Disapplying pre-emption rights – a statement of principles* ([www.pre-emptiongroup.org.uk/principles/index.htm](http://www.pre-emptiongroup.org.uk/principles/index.htm)), the Pre-Emption Group:

- says that section 80 authorities and section 95 disapplications should be granted for no more than 15 months or until the next AGM, whichever is shorter; and
- acknowledges that it treats treasury shares inconsistently when setting the cap on section 95 disapplications, recommending they be included when calculating the annual cap of 5 per cent of ordinary share capital but excluded when calculating the cumulative three-year cap of 7.5 per cent of ordinary share capital. It has deferred any amendment pending a planned BERR consultation on the statutory limits on holding treasury shares.

The ABI has reissued its model section 95 resolution to accord with the provisions of the Pre-Emption Group's statement of principles. The ABI asks companies to confirm that they intend to follow the provisions in the statement of principles regarding the cumulative three-year cap when asking shareholders to pass the resolution.

In July and November 2008 the Pre-Emption Group published monitoring reports analysing how its statement of principles has been applied since 2006. In the year to September 2008 over 600 requests to disapply pre-emption rights were put to shareholders by UK companies with a primary listing on the London Stock Exchange's Main Market, 13 per cent of which were for more than 5 per cent of ordinary share capital (a 1 per cent increase on the previous year). Three of these resolutions were rejected – all from investment vehicles – and four resolutions were adjourned rather than put to the vote. All other resolutions were approved.

#### **Political donations – effect of the extended rules**

Many companies ask shareholders to authorise political donations and expenditure at each AGM. In many cases the company does not intend to benefit a political party or cause, but takes the view that the legislation may still catch its actions. The 2006 Act's controls on political donations and expenditure are broadly the same as those in the 1985 Act and we expect these precautionary resolutions to continue. The ABI has asked companies when putting a precautionary resolution to shareholders to confirm that it is their policy not to make political donations and that they have no intention of using the authority for that purpose. The legislation allows authorisation of political donations and expenditure to be given for up to four years, but the ABI's guidance requires annual renewal.

There are some changes in the 2006 Act, most of which came into force in October 2007. From 1 October 2008, the scope of statutory control was extended to donations to, and expenditure on, independent candidates at any election to public office in the UK or any EU member state – previous rules applied only to support for political parties and organisations. Companies that have not already done so should consider whether to change the wording of the authorising resolution for the 2009 AGM if the current form of resolution does not cover donations or expenditure to independent candidates. Directors' reports relating to financial years

beginning on or after 6 April 2008 are required to contain details of donations to independent election candidates.

### **Auditors' limitation of liability**

Since 6 April 2008, companies have been able to agree a contractual limit on their auditors' liability to the company. The limit cannot be less than such amount as is fair and reasonable in all the circumstances. A separate agreement is required for each year's audit and each agreement must be approved by the company's shareholders.

The FRC has issued guidance on the application of these provisions – [www.frc.org.uk/about/auditorliability.cfm](http://www.frc.org.uk/about/auditorliability.cfm). It considers some of the factors that may be relevant to any decision by the directors on whether a company should enter into a liability limitation agreement, looks at which matters should be covered in the agreement (including specimen clauses for inclusion in a liability limitation agreement) and examines the process to be followed to seek shareholder approval for the agreement, including for subsidiaries (and provides specimen resolutions).

One of the key considerations when directors are assessing whether to recommend entering into a liability limitation agreement will be the likely views of shareholders. The Institutional Shareholders' Committee (ISC; including the ABI and NAPF) has issued a statement setting out what institutional investors are likely to expect from companies proposing to enter into an auditor liability limitation agreement – [www.frc.org.uk/about/auditorliability.cfm](http://www.frc.org.uk/about/auditorliability.cfm). In particular:

- agreements should be proportionate and provide a fair and reasonable limit on liability;
- companies should recognise that they are not obliged to enter into agreements if they are not suitable;
- companies should justify to shareholders the benefits of concluding agreements before putting them to a general meeting vote;
- audit committees should disclose in the annual report and AGM circular the ways in which they have used their discussions with auditors on liability limitation to assure themselves that audit quality will be preserved and enhanced, and to secure other benefits for the company;
- boards of holding companies should be prepared to disclose in the annual report and AGM circular what arrangements are being made in relation to subsidiary and joint venture companies; and
- shareholders will not want to see their preference for proportionate liability agreed at holding company level undermined by other forms of agreement lower down the group structure.

In its December 2008 guidance the ABI expressed support for the ISC statement. The November 2007 NAPF corporate governance guidelines suggest that investors should consider voting against resolutions that

propose any form of liability limitation other than proportional liability, unless there are 'compelling reasons why that is not appropriate' and 'why the directors feel that another form of liability limitation would survive a court's judgement of what is fair and reasonable'. Pensions and Investment Research Consultants (PIRC) has stated that it is not in favour of the limitation liability agreements and that its voting recommendations will be decided on a case-by-case basis.

In January 2009 the GC100 published a note summarising the issues for companies to consider, drawn principally from the FRC guidance and the ISC statement – [www.practicallaw.com/7-384-6267](http://www.practicallaw.com/7-384-6267). It suggests in particular that:

- in deciding to recommend a limitation agreement to shareholders for approval, directors must be satisfied that entering into the agreement would accord with their duty to promote the company's success;
- companies should see the limitation agreement in the context of the existing contractual relationship that they have with the auditors – normally an engagement letter and letters of representation – which may themselves limit the auditors' liability; and
- it is reasonable that auditors should bear the costs of any research necessary to establish how to deal with limitation of liability in the case of complex groups consisting of large numbers of companies spread over many jurisdictions.

It will be important that companies engage in early discussion with investors about proposed agreements and disclose how limitation of auditors' liability will apply throughout the group. The ISC expects companies to use the specimen principal terms set out in the FRC's guidance – companies choosing not to will need to consult early with shareholders.

As mentioned in Part 2 above, the principal terms of the limitation agreement must be disclosed in the notes to the company's accounts for the relevant financial year.

UK companies with listings outside the UK should consider whether any laws and regulations of other countries affect their ability to enter into limited liability arrangements. In particular, the SEC does not currently permit such agreements. The FRC has been discussing the position with the SEC but no statement has yet been made.

## Part 4 – AGM documents and procedures: 2009 onwards

### Key changes already in force

- Additional information in AGM notice – eg proxy rights, indirect holders' rights, ICOSA procedures on multiple corporate representatives.
- Explaining and publicising changes to articles – applying the FSA rules.
- Audit concerns – shareholders' right to require website statement.
- New rules on requisitioned resolutions and shareholders' statements – company pays costs if received by financial year-end.
- Proxies and corporate representatives – new voting rules.
- Publishing voting results on the website.

### Key changes for traded companies from August 2009 (based on the Draft Regulations)<sup>1</sup>

- Annual resolution must be passed from 2009 onwards to call other general meetings on 14 days' notice.
- Additional information required in the notice of general meeting.
- Electronic address in the proxy form.
- Documents and information – including the proxy form – must be published on the website before the general meeting and certain information must be added after the notice is sent out.
- Shareholders can requisition a resolution up to 14 days before an AGM.
- Company must pay the costs of requisitioned AGM resolutions.
- Shareholders have new right to add items to the AGM agenda up to 14 days before the AGM – revised notice must be sent out at least one week before the AGM.
- Electronic meetings and voting are permitted.
- Company must answer shareholders' questions at a general meeting.
- Company must publish additional information on poll results on the website.

### Key changes for all companies from August 2009 (based on the Draft Regulations)<sup>1</sup>

- Shareholders can vote in advance – by post or in electronic form – if articles allow.
- Corporate representatives can vote in different ways from one another in respect of different blocks of shares.
- New rules apply when a shareholder's proxy casts votes for different shares in different ways.
- Statutory requirement for proxy to act in accordance with any instructions given by the member appointing him.
- Shareholders with 5 per cent of share capital can require the directors to call a general meeting – this used to be 10 per cent.

### Introduction

The 2006 Act contains a number of requirements that affect AGMs – in particular those of quoted companies – designed to promote accessibility of information for shareholders and the public in general. Most of these came

<sup>1</sup> The final form of the Draft Regulations may differ from what is set out below.

into force on 1 October 2007 or 6 April 2008. There have been many changes to procedures, documentation and website content, some of which are mentioned below. The FSA has also clarified some aspects of its requirements on circulars. The Draft Regulations will make other significant changes with effect from 3 August 2009.

### **Content of AGM notice/circular – existing requirements**

As from 1 October 2007 the 2006 Act has required changes to the content of the AGM notice. For example, additional information on proxy rights must be included in the notice of meeting. It is important that a company does not unintentionally put itself in the situation where it is taken to have agreed to receive documents in electronic form simply by specifying an email address, telephone or fax number or website in a notice of meeting or proxy form. The DTRs require a statement of total voting rights to be included in the notice of meeting.

Specific wording is required on general meeting notices sent to nominated persons. Whether companies choose to produce two versions of the notice (one for registered shareholders and one for nominated persons) or a combined version is left to them to decide, weighing up cost savings against potential confusion. Most companies issue a combined version.

The version sent to nominated persons must state that he or she may have the right to be appointed, or have someone else appointed, as a proxy for the meeting and, if he or she has no such right or does not wish to exercise it, may have a right to give voting instructions to the registered shareholder. The required statement to the registered shareholder that he or she can appoint a proxy must either be omitted in the version sent to a nominated shareholder or, if it is included, also state that it does not apply to the nominated person.

For extra information to be given to shareholders when they are asked to pass resolutions about share allotment authorities, please see ‘Issuing shares – directors’ authority and disapplying pre-emption rights’ in Part 3 of this guide. In particular, the ABI requires companies asking shareholders to pass a section 95 resolution to confirm that they intend to follow the Pre-Emption Group’s requirements on the cumulative three-year cap (see its December 2008 guidance – [www.ivis.co.uk/ShareholdersPreemptionRight.aspx](http://www.ivis.co.uk/ShareholdersPreemptionRight.aspx)).

In issue 17 of its newsletter *List!* the FSA advises that:

- circulars sent to shareholders regarding changes to be made to the articles to take account of the 2006 Act do not need to be vetted by the FSA unless they contain unusual features;
- the circular will contain unusual features if the changes to the articles are unusual; and
- companies should contact the FSA helpdesk if they are unsure whether planned changes to their articles are unusual.

A working group of several city law firms has developed a pro forma circular to shareholders explaining the typical changes to articles that companies may want to make to reflect the 2006 Act and the short notice resolution discussed in 'Permitting short notice for general meetings' in Part 3 – [www.citysolicitors.org.uk](http://www.citysolicitors.org.uk). The document includes the AGM notice. The FSA has confirmed that the changes summarised in the pro forma circular can be regarded as not containing unusual features and so do not need to be approved by the FSA.

The FSA's rules were amended with effect from 20 January 2007 to require a company proposing any amendment to its articles – even if there is no unusual feature – to communicate the draft amendment to the FSA and the relevant regulated market without delay, but at the latest on the date of calling the relevant general meeting. The FSA has indicated that a simple statement that amended articles (preferably a blacklined version) are available for inspection on the FSA's document viewing facility is sufficient.

#### **Content of AGM notice and circular – changes from August 2009<sup>2</sup>**

From 3 August 2009 the Draft Regulations will require a traded company's notice of general meeting to include (in addition to the information the 2006 Act, the DTRs and the articles already require):

- a statement giving details of the website on which the information that must be published before the meeting is available (see 'Website publication of information before a general meeting – changes from August 2009' below);
- a statement of the 'precise procedures' with which members must comply to be able to attend and vote at the meeting (including the date by which they must comply);
- a statement (a) that the right to vote at the meeting is determined by reference to the register of members and (b) of the time when that right is determined in accordance with the 2006 Act (see 'Record dates and abolishing share-blocking – changes from August 2009' below);
- any forms to be used to appoint a proxy (see below for potential problems this may cause);
- if the company offers the facility for members to vote in advance (see 'Advance voting on a poll' in Part 3 above) or by electronic means (see 'Electronic meetings and voting' below), (a) a statement of the 'precise procedures' for doing so (including the date by which it must be done) and (b) any forms to be used; and

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<sup>2</sup> The final form of the Draft Regulations may differ from what is set out below.

- a statement of members' right to ask questions (see 'Shareholders' questions – changes from August 2009' below).

If the meeting is an AGM the notice must also include a statement of the shareholders' rights to require the company to:

- give notice of a resolution to be moved at the meeting (see 'Requisitioned resolutions and shareholders' statements – changes from August 2009' below); and
- include a matter in the business to be dealt with at the meeting (see 'Requisitioned resolutions and shareholders' statements – changes from August 2009' below).

### **Website publication of information before a general meeting – changes from August 2009**

The Draft Regulations will require a traded company to publish the following information on a website before a general meeting:

- the notice of the meeting;
- the total numbers (as at the latest practicable time before the notice is sent) of shares in the company and shares of each class in respect of which members are entitled to exercise voting rights at the meeting; and
- the totals (as at the latest practicable time before the notice is sent) of the voting rights that members are entitled to exercise at the meeting in respect of the shares of each class.

This information must be available on the website throughout the period beginning with the first date on which notice of the meeting is sent and ending with the conclusion of the meeting. Failure to meet this requirement will be a criminal offence, but will not affect the validity of a meeting or anything done at it. Any shareholders' statements, shareholders' resolutions or matters of business received after the notice is published must be published as soon as reasonably practicable and be available on the website for the remainder of the period.

Currently, the 2006 Act requires website publication of the meeting notice only if the company chooses to give notice of a meeting by means of a website following the procedures set out in the 2006 Act – although many traded companies make the notice available on their websites as a matter of good practice.

### **Communications with shareholders**

It has been reported that about half of the FTSE 350 companies have written to shareholders seeking their consent to electronic communications. The number of shareholders who respond asking for hard copy documents varies considerably – up to about a third of shareholders in some cases. In its newsletter *List!* 17 the FSA said that any letter of this type sent to shareholders falls within the Listing Rules definition of a circular and so must comply with the Listing Rules' content requirements. But the FSA

concedes that it may not be appropriate to include the required statement asking shareholders to pass on the document to the new holder when all the shares have been sold or transferred if the letter is personalised and contains information specific to the shareholder that may be sensitive and confidential.

#### **Audit concerns**

New rules in force on 6 April 2008 permit shareholders of quoted companies to require the company to publish a statement on a website setting out any matter that the members propose to raise at the next AGM regarding:

- the audit of the company's accounts (for financial years beginning on or after 6 April 2008) that are to be laid before the next AGM; or
- any circumstances connected with an auditor of the company ceasing to hold office since the last AGM (applicable to auditors appointed for financial years beginning on or after 6 April 2008).

The same minimum shareholder requirements apply as for poll scrutiny requests (see 'Voting on a poll – existing rules' below). Companies must give certain information about these rules in the AGM notice (but not if the accounts to be laid are for, or the relevant auditor was appointed for, a financial year beginning before 6 April 2008).

#### **Requisitioned resolutions and shareholders' statements – existing rules**

As from 1 October 2007, public companies (not only those with traded securities) must, in certain circumstances, pay the cost of circulating shareholders' resolutions for an AGM if the shareholders' request is received before the company's financial year-end. The same minimum shareholder requirements apply as for poll scrutiny requests (see 'Voting on a poll – existing rules' below). Requests can be in hard copy or electronic form.

As from 1 October 2007, companies (public and private) must in certain circumstances pay the cost of circulating shareholders' statements regarding business at an AGM if the shareholders' request is received before the company's financial year-end. The same minimum shareholder requirements apply and requests can again be in hard copy or electronic form.

#### **Requisitioned resolutions and shareholders' statements – changes from August 2009**

The Draft Regulations as currently proposed will change the deadline for members' requests to the company to give notice of a resolution for the next AGM to 14 days before the meeting (if the company is a traded company). Under current rules, the request must be received not later than six weeks before the AGM or, if later, the time at which notice is given. Companies may feel the deadline period is rather short, particularly if there are large numbers of shareholders. The Draft Regulations will require the company to meet the cost of circulating the members' resolution in all circumstances –

now, the company is required to pay only if the request is received before the end of the financial year preceding the AGM.

The Draft Regulations will give members of a traded company a new right to require the company to include a matter in the business to be dealt with at an AGM. This is distinct from the right to propose a resolution – see above. The same minimum shareholder requirements apply as for poll scrutiny requests (see ‘Voting on a poll – existing rules’ below).

The request (in hard copy or electronic form) must identify the matter to be included in the business, be authenticated by the person or persons making it and be received at least 14 days before the AGM. The company must send a revised AGM notice to everyone who received the original notice at least one week before the AGM and by the same means. It must also publish it on the same website as that on which it publishes the other information required by the Draft Regulations – see ‘Website publication of information before a general meeting – changes from August 2009’ above.

Companies may feel the 14-day deadline is rather short, particularly in view of the proposed obligation to send a revised AGM notice at least one week before the AGM. The Directive does not set the one-week requirement but requires the revised notice to be made available either before the record date set for voting at the meeting or, if there is no such date, far enough before the meeting to enable shareholders to appoint a proxy or vote by correspondence (see ‘Advance voting on a poll’ in Part 3 above).

#### **Exercise of rights if shares are held for others**

If certain conditions are met, the 2006 Act allows indirect investors to be counted in calculating whether the shareholder threshold has been reached to trigger valid members’ requests for independent reports on polls, publication of audit concerns (see ‘Audit concerns’ above), requisitioned resolutions and circulation of statements.

#### **Inspection of directors’ service contracts**

The Combined Code requires the terms and conditions of appointment of non-executive directors to be made available for inspection at the AGM, but NAPF corporate governance guidelines extend this to all directors’ service contracts.

#### **Proxies and corporate representatives – existing rules**

Detailed rules in the 2006 Act on the number of votes a proxy is entitled to exercise at the meeting came into force on 1 October 2007. Forms of proxy must therefore provide for the appointment of multiple proxies representing different numbers of shares.

The Combined Code also has an effect on proxies. It requires:

- a ‘vote withheld’ box on AGM proxy forms;
- publication of the details of proxies lodged at the AGM if votes are taken on a show of hands; and

- the proxy form and any announcement of results of a vote to make clear that a vote withheld is not a vote in law and will not be counted in the calculation of votes.

As mentioned in Part 3, institutional investor groups have continued to express concern over the 2006 Act's provision that, if a corporate shareholder appoints more than one representative and they exercise the same power (such as voting) in different ways, the power is treated as not being exercised. They are looking to companies to follow the best practice guidance issued by ICSA on dealing with multiple corporate representatives at general meetings – see 'Proxies and corporate representatives' in Part 3 for more information – and the ABI has asked companies to confirm in the notes to their AGM notices that they will do so.

Institutional investor groups have expressed concern and the government has proposed alterations to this provision with effect from 3 August 2009 – see below. Companies should take care when amending any relevant provisions in their articles.

#### **Proxies and corporate representatives – changes from August 2009**

The Draft Regulations as currently proposed will mean that a company will only be able to require a member appointing a proxy to provide reasonable evidence of (a) the identity of the member and of the proxy and (b) the member's instructions (if any) on how the proxy is to vote. This is unlikely to change UK practice but will be helpful to shareholders in other member states, where formal requirements such as notarisation or an apostil are sometimes required.

A traded company will have to give an electronic address in every instrument of proxy sent out for the purposes of a general meeting of the company and every invitation to appoint a proxy issued for the purposes of such a meeting. This will trigger the 2006 Act's existing provision that the company is deemed, by providing an electronic address, to have agreed that any document or information relating to proxies for that meeting may be sent by electronic means to that address (subject to any conditions or limitations specified in the notice). The requirement goes further than the Directive, which requires only that member states must allow shareholders to appoint proxies by electronic means and companies to accept electronic notifications of proxy appointments and requires companies to offer at least one effective method of notifying proxy appointments by electronic means. The same requirements apply to revocations.

The Draft Regulations will require a company to include any forms to be used for the appointment of a proxy in the notice of the meeting. This means they will also be available on the company's website. This seems undesirable, because companies usually want proxy forms to be personalised so the registrars can identify the shareholder appointing the proxy. It goes further than the Directive requires, which allows forms not to be included if they are sent directly to each shareholder.

The Draft Regulations create a new statutory obligation on a proxy to act in accordance with any instructions given by the member appointing him or her. We would not expect to see this reflected in the articles. It is arguable whether the new obligation is needed, because the general law probably already requires the proxy to vote in accordance with instructions. However, the Draft Regulations do not make it clear that the result of a vote is not affected if a proxy votes other than in accordance with their instructions. As companies have no way of knowing whether a proxy is following instructions, it would be helpful to make this clear and to clarify what a shareholder's remedy is if the proxy does not follow instructions.

The 2006 Act will be amended to permit corporate representatives to vote in different ways from one another in respect of different blocks of shares.

#### **Voting on a show of hands – existing rules**

As the 2006 Act allows a registered shareholder to appoint more than one proxy (provided each proxy represents a different part of the registered holding), it is possible on a show of hands for there to be more than one vote per registered holding in the room. If the chairman considers the number of proxies appointed by a single registered shareholder to be affecting the outcome of a vote on a show of hands, he or she should call a poll.

A chairman's casting vote in the event of equality of votes on a show of hands is no longer effective under the 2006 Act. There is an exception if, immediately before 1 October 2007, the company's articles made provision for a casting vote. If the casting vote has already been removed from the articles as a result of the 2006 Act, the company may at any time restore that provision to take advantage of this saving provision. This is unlikely to be relevant to general meetings of a listed company.

#### **Voting on a show of hands – changes from August 2009**

The Draft Regulations propose changes to the 2006 Act to clarify the rules that apply when a shareholder's proxy casts votes for different shares in different ways. On a show of hands, a proxy appointed by one member will have one vote and a proxy appointed by more than one member will have one vote if instructed to vote in the same way by all those members. If instructed to vote in different ways, the proxy will have one vote for and one vote against. If a shareholder has appointed more than one proxy, all the proxies taken together will have one vote or one vote for and one against. This means companies will still face practical difficulties if a nominee holding for different beneficial owners has appointed two or more proxies.

A chairman's casting vote will no longer be effective in any circumstances.

The final form of the Draft Regulations may differ in the light of responses to the consultation on these points.

#### **Voting on a poll – existing rules**

The 2006 Act does not require all-poll voting on resolutions, but allows shareholders in quoted companies to require independent scrutiny of a poll

in certain circumstances. This requirement came into force on 1 October 2007. To trigger the independent scrutiny requirements, requests must be made by:

- members representing not less than 5 per cent of the total voting rights of all members who have a right to vote on the matter to which the poll relates; or
- not less than 100 members with the right to vote on the matter to which the poll relates and who hold shares in the company on which an average sum per member of not less than £100 has been paid up.

The requests may be made before or up to one week after the meeting. If an independent report is requested, the directors must appoint an independent assessor (for example, the company's auditor – but not the registrar) within one week of the request for a report. The 2006 Act does not set out the scrutiny procedure, nor the consequences of an adverse assessment. The independent assessor's identity, a description of the poll's subject matter and a copy of his or her report must be made available on the website.

The first exercise of the new shareholders' power to require directors to obtain an independent report on a poll took place in May 2008. Aegis appointed Electoral Reform Services as independent assessor to produce a report on polls taken at its AGM. The assessor confirmed that the procedures adopted in connection with the polls were adequate.

Companies may want to set up a response plan to deal with poll scrutiny requests.

### **Voting on a poll – changes from August 2009**

The Draft Regulations will allow shareholders to vote by correspondence – electronic or by post – if the company's articles allow. Members can already appoint proxies electronically and by post, but the Directive requires member states to allow companies to give shareholders the option to vote directly in advance without appointing a proxy. Under current rules, a vote can be cast by proxy only if the proxy holder is present at the meeting to cast it.

The Draft Regulations will permit a company's articles to contain a provision to the effect that, for a vote on a resolution on a poll taken at a meeting, the votes may include votes cast in advance. The government has asked for views on whether the right to demand a poll should also be exercisable in advance. Arguably, the Draft Regulations should also allow votes to be cast in advance if they are taken on a show of hands. A traded company is subject to the extra requirement that it can add conditions to exercising this right only if they are necessary to ensure the person voting is identified – and the conditions must be proportionate to achieving that objective.

If a company includes this type of provision in its articles, it will not be able to require the advance vote to be registered, broadly, more than 48 hours before the time for holding the meeting (ignoring working days).

We do not expect companies to take advantage of this new provision.

### **Record dates and abolishing share-blocking – changes from August 2009**

Share-blocking is a procedure in which, on a specific date before a company meeting, shareholders must notify the company of their identity and intention to vote. The shares involved cannot be traded after this date. Share-blocking does not occur in the UK, but it is not unlawful, so the law is being amended to prevent it.

The Directive requires a record date system – as already used in the UK – under which shareholders or their proxies are validated for voting at the meeting on a fixed date before the meeting, but allowing shares to be traded after this date. In general, UK companies set a record date of 48 hours before the meeting. If a company cannot determine the right to vote by reference to its register of members on the day of the meeting it must use a record date 48 hours before the time for holding the meeting. If it can do so, it can set a record date at any time up to 48 hours before the meeting. Non-working days must be ignored in calculating the relevant periods.

The Draft Regulations will allow companies that can use their register on the meeting day to determine the right to vote to use a record time 48 hours before the meeting, as permitted by the Uncertificated Securities Regulations. It would be helpful if those regulations were amended to allow non-working days to be ignored. The Draft Regulations have requirements only for a record date to attend and vote at a meeting and do not require the company to set a record date for receiving notice of the meeting.

### **Electronic meetings and voting**

In August 2009 the Draft Regulations will state that shareholders' meetings of all types of companies can be conducted by electronic means if those who participate can speak and vote. A traded company can only impose requirements and restrictions that are necessary to ensure the identification of those taking part and the security of the electronic communication – so long as they are proportionate to achieving those objectives.

### **Shareholders' questions – changes from August 2009**

The orderly conduct of the meeting will continue to be the chairman's responsibility, within the bounds of the company's articles and the common law. This will be subject to a new statutory obligation on the company to answer any question about the business being dealt with at the meeting put by a member attending the meeting. The Draft Regulations as currently drafted do not make it clear whether a proxy or corporate representative attending the meeting for a member can also require an answer to their question – although this is probably the intention.

The company does not need to answer a question if:

- doing so would interfere unduly with the preparation for the meeting or involve the disclosure of confidential information;
- the answer has already been given on a website in the form of an answer to a question; or
- it appears to the chairman of the meeting that it is undesirable in the interests of good order of the meeting that the question be answered.

It is not clear why the Draft Regulations do not include an exemption for the protection of the company's business interests or make it clear that one overall answer may be given to questions with the same content – which the Directive permits. The final form of the Regulations may do this.

#### **Website publication of AGM outcome – existing rules**

Companies must ensure that they comply with the 2006 Act's website disclosure requirements. These include the obligation to publish:

- poll results;
- the report of any independent poll assessor (see 'Voting on a poll – existing rules' above);
- the company's annual report and accounts; and
- any statement of audit concerns (see 'Audit concerns' above).

The Combined Code's good practice standards will presumably continue to require the company to publish certain information about the results of a resolution taken on a show of hands on its website as soon as reasonably practicable.

PIRC does not consider that putting the results of polls on a company's own website is sufficient and requires full disclosure of proxy votes received, including abstentions.

#### **Website publication of voting results – changes from August 2009**

From August 2009 the Draft Regulations will require a traded company, if a poll is taken at its general meeting, to ensure that the following information is available on a website:

- the date of the meeting (no change to the 2006 Act's existing rules);
- the text of the resolution or, as the case may be, a description of the subject matter of the poll (no change);
- the number of votes validly cast;
- the proportion of the company's issued share capital at close of business on the day before the meeting represented by those votes;
- the number of votes cast in favour (no change);
- the number of votes cast against (no change); and

- the number of abstentions, if counted. (The Directive requires information on abstentions if applicable, rather than if counted.)

These requirements also apply to a meeting of holders of a class of shares in connection with the variation of the rights attached to the shares.

The company must publish this information not later than the end of the 15th day after the date of the meeting or, if later, the end of the first working day following the day on which the result of the poll is declared. In contrast, information required by the 2006 Act must be on the website as soon as reasonably practicable and be available for two years.

#### **Shareholders' power to require directors to call a general meeting**

In broad terms, the Draft Regulations will reduce the minimum share capital that members must hold to require the directors to call a general meeting from 10 to 5 per cent. This does not need to be set out in the articles.

## **Conclusion**

For most companies there will be a lot to think about. Please contact us if you would like to discuss specific points in more detail.

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