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Company fundamentals

Basic questions

1. What is a company?

The term 'company' is commonly used meaning some association of people, as in a touring theatre company. The actors may or may not be associated with a registered company, and might be just a group of friends who enjoy putting on plays. It is a term frequently used by unincorporated sole traders and by partnerships. Thus 'Bill Smith and Company' could denote a sole trader or partnership, and not necessarily a registered company.

There have been companies incorporated by charters granted by the Crown and companies incorporated under the authority of Acts of Parliament. The South Seas Company of bubble fame was an example of the former, and the early railway companies were examples of the latter. Since 1844 Britain has had facilities for people to incorporate companies formed under the authority of the Companies Acts and register them with the Registrar of Companies. These are usually what people have in mind when they talk about companies. There are now around 2,700,000 such companies and they form an essential part of the life of the country, and in particular of its economic activity. The questions and answers in this book relate almost exclusively to companies registered under the Companies Acts.

2. What are the different types of company?

They are the following:

- Public company limited by shares
- Private company limited by shares
- Private company limited by guarantee
- A company limited by guarantee and having a share capital
- Private unlimited company with share capital
- Private unlimited company without share capital

All public companies are limited by shares. All listed companies are public companies, although not all public companies are listed. All unlimited companies are private companies. Since 22nd December 1980 it has not been possible to register a new company limited by guarantee having a share capital.

3. What are the differences between public companies and private companies limited by shares?

Public companies must be limited by shares. They cannot be unlimited or limited by guarantee. Key differences include the following:

- The allotted value of the share capital of a public company must be at least £50,000, of which at least 25 per cent must be paid up. Any share premium must be 100 per cent paid up. There is no minimum sum for the share capital of a private company, although it cannot be NIL. In both public and private companies there is no maximum amount for the share capital.
- Only a public company can be a listed company.
- Only a public company can issue a prospectus and offer its shares to the public.

More differences are detailed in the answer to the next question.

4. Are there any more differences between public companies and private companies limited by shares?

Yes there are. There are many others, but they include:

- The name of a public company must end with the words 'Public Limited Company', the abbreviation 'PLC' or the Welsh language equivalents.
- Public companies have a shorter period than private companies to deliver their accounts to the members and the Registrar.
- Public companies must hold annual general meetings. It is optional in private companies.
- Public companies must have at least two directors. If permitted by their articles (which Table A does not), a private company may have a sole director.
- Written resolutions of the members are only available to private companies.
- There are different model articles.

5. Can a company start trading (or operating) as soon as it has been registered?

A private company can start trading (or operating) immediately. A public company may only do so when a certificate entitling it to commence trading has been issued by the Registrar. It should also be noted that it may not borrow until this certificate has been issued. Application for the certificate may be made on form SH50. It is a declaration that the value of the allotted share capital is at least £50,000, and it gives details of how the shares are paid up, preliminary expenses and any payments or benefits in favour of the promoter.

6. What exactly is meant when it is said that a company has a separate legal personality?

An incorporated company has a legal existence separate from the legal existence of its members. It can own property in its own name and it can sue and be sued in its own name. It can in some circumstances sue and

be sued by its members. The principle that a company has a legal existence separate from that of its members was confirmed by the case *Salomon v Salomon and Co Ltd 1897*, one of the most celebrated cases in company law and possibly well known to you.

7. Exactly what does limited liability mean?

In the context of this question limited liability means the liability of the members, not of the directors or others. The overwhelming majority of companies are limited liability companies, which means that the liability of the members is limited by shares or by guarantee. If a company is limited by shares, the liability of each member is limited by the full amount of the shares that he holds. Most shares are issued fully paid, so in the event of an insolvent liquidation the shares become worthless. If shares are partly paid, the members are liable to pay the uncalled part of their shares. If a company is limited by guarantee and it becomes insolvent, each member must contribute the amount of his guarantee.

8. Would you please give me some figures to show the expansion in the number of registered companies?

The concept of a private limited company dates back to 1907 and at that time there were less than 90,000 companies on the register. In recent years there has been an enormous increase in the number of companies on the active register. The figures (rounded to the nearest hundred) have been:

	England and Wales	Scotland	Total
31st March 1995	926,500	55,300	981,800
31st March 2000	1,288,200	73,200	1,361,400
31st January 2004	1,762,700	100,400	1,863,100

On 1st June 2008 the total number of companies registered in Britain was 2,460,770 of which 10,715 were public companies. The total number

of companies registered in the United Kingdom is now close to 2,700,000 of which approximately 40,000 are registered in Northern Ireland.

Around 99.6 per cent of companies are private companies and only 0.4 per cent are public companies. Although Scotland has around ten per cent of the population it only has around five per cent of the companies.

9. What are the alternatives to a company?

They include the following:

- Trading as a sole trader
- A general partnership
- A limited partnership
- A limited liability partnership (LLP)
- An unincorporated association
- A trust

Registration of companies

10. How is a company registered?

The following documents with the required fee must be submitted to the Registrar of Companies:

- A memorandum of association in the required form authenticated by at least one subscriber.
- Articles of association, unless it is intended that the company will exclusively use the model articles for that type of company.
- Form IN01 Application to register a company. This form supplies prescribed information to the Registrar.
- The formal approval of the name of the company (if required).

If everything is in order, the Registrar will issue a certificate of incorporation and place the company on the list of registered companies.

11. Is there a quick, cheap and easy way of getting my own company?

You should probably approach a company formation agent. These agents register and provide so called off-the-shelf companies. They register batches of companies with standard features, with them and their staff as the directors. The companies are kept dormant. On application from you they will change the name (if required), the registered office, and the directors. They will also make any other required changes. Unless something out of the ordinary is wanted the whole thing should cost less than a hundred pounds, plus the amount paid for the shares of course.

12. Is it possible to change a company's form of registration?

A company with a share capital still cannot re-register as a company limited by guarantee, and a company limited by guarantee still cannot re-register as a company with a share capital. Subject to complying with the correct procedures (which vary) the following are possible:

- A private company (limited or unlimited) with shares can become a public company limited by shares.
- A public company limited by shares can become a private company limited by shares.
- An unlimited company can become a private company limited by shares or by guarantee.
- A private company limited by shares or by guarantee can become an unlimited company.
- A public company limited by shares can become a private unlimited company.

13. Can a company registered in England and Wales change its place of registration to Scotland?

No this is not possible, and neither can a company registered in Scotland change its place of registration to England and Wales. What you can do is register a new company in Scotland, then sell or transfer the first company's assets and business to it. Then the first company can be wound up or struck-off. Its name should then be available and the

Scottish company should be able to change its name to that of the first company.

Companies limited by shares

14. What are the essential features of a company limited by shares?

Around 97 per cent of companies are limited by shares. They are either PLCs or private companies limited by shares. The obvious point to make is that in the event of the company becoming insolvent the liability of the members for the company's debts is limited by the amount of the shares that they hold. Their shares become worthless and they must pay up any unpaid sums on the shares, but that is the limit of their liability.

The fact that there are shares means that there is the prospect of the members receiving dividends. There is a lot of law about shares, share capital and dividends, and the provisions of the articles will be very relevant. Table A is the model set of articles for a public or private company registered before 1st October 2009 that is limited by shares. New model articles took effect from 1st October 2009 for companies registered from that date. From 1st October 2009 there are separate model articles for public companies and for private companies limited by shares.

Unlimited companies

15. What are the essential features of an unlimited company?

The principal and obvious feature is that the members have unlimited joint and several liability for the company's debts. There are no prescribed model articles for unlimited companies registered from 1st October 2009. For unlimited companies registered before that date it is Table E. Most unlimited companies are not required to file their accounts with the Registrar, though they must do so if the company is a holding company or subsidiary of a limited company.

16. What sort of organisation might suit being an unlimited company?

Given the potential liability, such companies tend to be relatively small where the members can keep a close eye on them. They are sometimes used by professional practices as an alternative to partnerships.

17. Why would anyone in their right mind agree to be a member of an unlimited company?

Given the potential unlimited joint and several liability your question is understandable, and there are only around five thousand unlimited companies registered in the United Kingdom. One reason could be that the members want the world to know that they have total confidence in the company – it should impress the bank manager if the company asks for a loan. The members could be people who might be attracted to a general partnership, where the partners have unlimited liability, but want the structure of a company and company law.

Companies limited by guarantee

18. What are the essential features of a company limited by guarantee?

The members do not own shares with the consequence that dividends cannot be paid. Profits (or more accurately surpluses) are invested, retained in the company or spent in furtherance of the objects of the company. When the company is wound up the net assets are not paid to the members, but distributed according to the objects and constitution of the company.

The members comprise the subscribers to the memorandum and such other persons as the directors approve for admission to membership. Each member signs a guarantee that in the event of the company becoming insolvent, he will contribute up to a specified sum. The amount of the guarantee is frequently nominal, such as, for example, ten members agreeing to contribute up to one pound each.

19. Are there minimum or maximum amounts for the guarantees in a company limited by guarantee?

No.

20. What sort of organisation might suit being a company limited by guarantee?

Companies limited by guarantee are often charitable organisations. They may also appeal to sports associations, trade associations, flat management companies, and Chambers of Commerce among others.

Community interest companies

21. What is a community interest company?

A Community Interest Company must have 'Community Interest Company' or 'CIC' at the end of its name, so it could be, for example, 'Bognor Regis Affordable Childcare CIC Ltd'. It is possible for a community interest company to be a PLC, a company limited by guarantee or a private company limited by shares. Most of them are private companies limited by guarantee.

22. Please tell me more about community interest companies?

The distinguishing features of a Community Interest Company include the following:

1. It must show that it will pursue purposes beneficial to the community and not an unduly restricted group of beneficiaries.
2. Regulations permit the exclusion of companies with certain objectives. Political parties and political campaigning organisations are examples.
3. A CIC is not able to have charitable status. However, charities are able to have CICs as subsidiaries.

4. A CIC is required to produce an annual community interest company report. This is publicly available at Companies House.
5. A CIC is prohibited from distributing any profits to its members. However, a CIC that is limited by shares does have the option of issuing dividend-paying "investor shares". The dividends payable on such shares are subject to a cap.
6. When a CIC is wound up its residual assets are not distributed to its members, as in the case of a normal company. Instead, they pass to another suitable organisation that has restrictions on the distribution of its profits, for example another CIC or a charity.
7. A regulator has been appointed to police and generally supervise CICs. The regulator approves applications for CIC status and has powers to investigate alleged abuses of CIC status. He can remove directors, freeze assets and apply to the court for a CIC to be wound up.
8. A CIC has none of the benefits or burdens of charitable status. It is not subject to regulation by the Charity Commission or the charitable jurisdiction of the High Court.

23. What sort of companies might be community interest companies?

A Community Interest Company is a non-profit distributing enterprise, but it is not an option for a registered charity or a political party. It may, for example, be suitable for businesses operating in such areas as childcare, social housing, leisure and community transport. The special characteristics of the CIC are intended to make it a particularly suitable vehicle for some types of social enterprise – essentially, those that wish to work for community benefit within the relative freedom of the non-charitable company form, but with a clear assurance of non-profit-distribution status.

Shareholder agreements

24. Is it possible to have a shareholder agreement separate from the articles?

Yes it is and it is quite common.

25. What is the point of shareholder agreements?

Shareholder agreements operate in addition to the articles of association. If well drafted they bind the shareholders that are party to them and this can be all of the shareholders. They may regulate the relationship of the shareholders and give rights and obligations that could not be put into the articles, or would not be appropriate for inclusion in the articles. For example a shareholder agreement could give a minority shareholder the right to have a director of his choice on the board. It might be difficult or impossible to engineer this through the articles and there may not be the necessary level of support to change the articles. Shareholder agreements can be kept confidential, but this is not possible for the articles. The company itself can be a party to a shareholder agreement.

26. What sort of things might be suitable for inclusion in a shareholder agreement?

A minority shareholder in a private company can find himself effectively 'locked-in'. He may disagree with the direction that the company is taking, but the majority decides and he could be perpetually outvoted. It may be difficult or impossible to sell his shares because any buyer would face the same problems. A shareholder agreement might overcome this difficulty by providing a basis for the valuation of the shares, and by providing an opportunity or compulsion for the other shareholders to buy them. It can also give the other shareholders first refusal.

There are many other possibilities. They include the right to be a director or have a nominated person as a director and the right to act as a consultant. They can include such things as the obligations of the shareholders to provide loan finance if it is needed.

Execution of documents and the company seal

27. What documents must be executed?

Deeds, contracts without consideration, share certificates and certain other documents must be executed as a deed.

28. How are documents executed?

Section 44 of the Act reads (in part) as follows:

> *'(1) Under the law of England and Wales or Northern Ireland a document is executed by a company –*
>
> *(a) by the affixing of its common seal, or*
>
> *(b) by signature in accordance with the following provisions.*
>
> *(2) A document is validly executed by a company if it is signed on behalf of the company –*
>
> *(a) by two authorised signatories, or*
>
> *(b) by a director of the company in the presence of a witness who attests the signature.*
>
> *(3) The following are "authorised signatories" for the purposes of subsection (2) –*
>
> *(a) every director of the company, and*
>
> *(b) in the case of a private company with a secretary or a public company, the secretary (or any joint secretary) of the company.*
>
> *(4) A document signed in accordance with subsection (2) and expressed, in whatever words, to be executed by the company, has the same effect as if executed under the common seal of the company.'*

Until 6th April 2008 it was a requirement that two persons signed when a document was executed. Since that date it has been possible, in any company, for one person to sign.

29. What is a suitable form of words when a company seal is not used?

If a document is intended to be a deed, and whose wording makes that fact clear, it will upon delivery have the effect of a deed. An example of such wording is:

Executed by …… Ltd as a deed and signed by

…… Director

…… Company Secretary

30. Is it compulsory for a company to have a company seal?

No it is not compulsory, though it was until 30th July 1990. However, many companies choose to still have and use a company seal, even though it is no longer a requirement.

There are now three possibilities:

- A company can have a company seal and use it.
- A company can decide not to have a company seal and use a suitable form of words instead.
- A company can have a company seal but, on some or all occasions when its use would be required, elect to use a suitable form of words instead.

31. Who may sign when the company seal is used?

Signature or signatures must be in accordance with the articles. It should be noted that Table A differs from the model articles that apply from 1st October 2009.

32. What records should be kept of the use of the company seal?

The use of the company seal should be approved by the directors, or a committee of the directors, and this should be evidenced by a retrospective board minute that identifies the document on which the seal was used. If the company seal is used a lot, it is not desirable to have a string of individual board minutes. Instead all the uses should be entered in a Sealings Register. Blocks of entries in the register can then from time to time be approved by the directors and these decisions should be minuted.

The requirements concerning directors' approval, minutes and a sealing register are exactly the same if a form of words is used instead of the company seal.

Officers of the company

33. Who is an officer of the company?

Section 1261 of the Act defines an officer as follows:

'in relation to a body corporate, includes a director, a manager, a secretary or, where the affairs of the body are managed by its members, a member.'

This is not a very satisfactory definition because the term 'manager' is not defined, and the word 'includes' poses the obvious question of who else might be considered an officer.

All directors (including non-executive directors) are always officers, and so are all company secretaries. A company's auditor is an officer for just some purposes. The position of managers varies according to circumstances. If there is an active board of directors running the company on a day to day basis, the managers would probably not be held to be officers. On the other hand, if the board is totally non-executive, a general manager with day to day control would almost certainly be an officer.

34. What are the consequences of being an officer of the company?

Officers have special responsibilities for trying to ensure that the company complies with company law. The Act is peppered with many references to the term 'officer', and it gives them certain rights and many responsibilities. Various other Acts also give responsibilities to officers. The officers of a company are accountable for it and what it does. The Act provides many offences that can be committed by officers. Just one example is section 162 which relates to the register of directors. Subsection (6) reads as follows:

'If default is made in complying with subsection (1), (2) or (3) or if default is made for 14 days in complying with subsection (4), or if an inspection required under subsection (5) is refused, an offence is committed by –

(a) the company, and

(b) every officer of the company who is in default.

For this purpose a shadow director is treated as an officer of the company.'

Just one example from another Act is section 212 of the Insolvency Act which relates to the penalisation of directors and officers. It specifically relates to (among others) *'a person who is or has been an officer of the company'*.

On a different tack, a company's financial statements must disclose certain transactions with its officers.

35. Can all officers commit all the offences?

No – some offences can only be committed by the directors. For example, the directors are required to prepare proper accounts, formally approve them and one director must sign the balance sheet. Only a director can sign the balance sheet and only the directors commit an offence if it is not done.

36. I am an officer of the company and it all sounds rather worrying. How worried should I be?

You should certainly take your responsibilities seriously but perhaps you should not worry too much. The great majority of officers manage without too many problems. You might take comfort from Section 1121(3) of the Act which states:

> *'An officer is "in default" for the purposes of the provision if he authorises or permits, participates in, or fails to take all reasonable steps to prevent the contravention.'*

Directors are required to take all reasonable steps.

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Company registration and company constitution