

# Firms should act now to sort out their constitution



**Pamela Abbott**

IN MANY ways the operation of a limited company is similar to that of our country – the directors are the “elected” agents of the shareholders, just as the government is that of the voting public. Each is then given the task of running the company and the country respectively in a way that best suits the interests of those it represents.

The difference is that with limited companies, the shareholders can step up and change how things are being run without having to wait for the directors to call a general election – arguably a much more democratic system.

For most companies these very powerful rights are enshrined, just like that of the voting public, in their constitution. 1 October, 2009 saw the final major raft of provisions of the Companies Act 2006 coming into force, signalling this is now the time for all limited companies to consider the impact this legislation has on their constitutions.

UK company law has traditionally been written with the large company in mind. The intention with the Act was to achieve a better balance for companies of all sizes through measures which streamline and simplify their constitutions.

New powers are now at the disposal of shareholders, directors and limited companies more generally to take advantage of the simplification measures, but they have some work to do to achieve this.

The constitution of a company is comprised of the documents which the shareholders sign up to which regulate the external and internal aspects of the company's activity. Traditionally there have been two documents, the memorandum of association and the articles of association.

The memorandum of association was the fundamental and unalterable document of the company which governed the company's relationship with the wider world. It set out the aims, or objects, of the company. The company was then restricted to carrying out only activities in pursuit of those aims. The objects in place at incorporation would indefinitely restrict the company to working within those confines. The articles of association by contrast provided the framework for the manage-

ment of the affairs of the company and the conduct of its business. This could be altered by the shareholders.

Now, in a sweeping change, a limited company's constitution will comprise the articles only. The memorandum will be a snapshot of limited information as at incorporation and, for any company incorporated after 1 October 2009, its objects will be unlimited, unless it chooses to restrict them in the articles. For existing companies their current restrictions will be deemed to form part of the articles; they will need to remove them to avoid being bound by them.

The Act makes changes in a large number of areas where the articles come into play. These include allowing directors to authorise conflicts of interest; changing the procedure for shareholders to make decisions in writing; removing the concept of a ceiling being placed on a company's share capital; communicating with shareholders electronically; removing the company secretary and changing notice periods for holding and making decisions at meetings of the shareholders.

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In many cases existing companies' articles will be more restrictive than the Act now requires. In order to take full advantage of the new provisions, changes to

the articles will be needed. In certain areas the Act overrides conflicting provisions in the articles, which should be altered so as to avoid confusion and inconsistencies.

While the reforms are certainly beneficial, the government can be criticised for failing to take the opportunity to stress to those running limited companies the importance of tailoring the terms of their companies' constitutions to cater for their specific business needs. Many limited companies will be operating with what are commonly referred to as “off-the-shelf” constitutions; those which have not been tailored to their business's individual requirements.

The aims and context of every company in the UK is different and the message is that one size does not fit all and advice should be taken as to the most appropriate terms to be contained in the company's constitution.

This is the ideal opportunity for companies to do just that; to take advantage of the changes in the law and at the same time create a regulatory framework which best suits their specific needs.

● Pamela Abbott is a solicitor with CCW Business Lawyers.