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Wishing you all a Merry Christmas and a Happy and Prosperous New Year

Money Laundering Reporting Officer (“MLRO”) Fined £17,500

The Financial Services Authority (FSA) has issued a £17,500 fine to the MLRO of a corporate advisory firm.

The fine was levied because the officer in question did not have adequate systems and controls in place for verifying and recording client identity.

The FSA also fined the firm (Sindicatum Holdings) where the MLRO worked for procedural failings in verifying the identity of its clients.

The case breaks new ground as it is the first time the FSA has fined an individual MLRO, although no evidence of money laundering came to light during the FSA enquiries.

Abolition of financial assistance – need for independent accountants review

The Law Society has published a paper “The implications for leveraged transactions of the repeal of the statutory prohibition of financial assistance by private companies”.

The abolition of the prohibition of financial assistance also makes the auditors “whitewash” redundant.

There has been discussion of whether, notwithstanding the repeal of the need for a whitewash, directors should nonetheless obtain the equivalent of a whitewash report from an independent accountant.

The Law Society Paper clarifies that directors should not normally need to request a review by an independent accountant of the cashflows and projections relied on when considering the net assets position of the company. It also states that directors may have an ongoing dialogue with the company’s auditors/accountants regarding the fact that any reduction in the net assets of the company as a result of providing financial assistance is covered by distributable reserves to make sure the auditor/accountant is comfortable with the directors assessment. However, there is no recommendation that independent accountants are requested to provide comfort to the directors regarding the distributable profits position.

The effect on net assets should be determined according to normal accounting principles, so that if the transaction does not require an immediate loss to be recognised there will be no effect on net assets. Accordingly the effect of an upstream guarantee, the creation of upstream security or the granting of an upstream loan will only be relevant if an immediate liability has to be recognised as a result.

If there is a risk that the transaction could result in a deficit in distributable reserves, further analysis will be required to determine whether the transaction could later be challenged as an unlawful reduction in capital or an unlawful distribution.

The ICAEW supports this paper and hopes that it will prevent companies (or their banks) requesting the involvement of independent accountants as a matter of course, which would be costly and negate the benefit of this reform.

The paper also states that the board minutes approving the financial assistance should be prepared which identify why it is in the best interests of the company and give the board's assessment of the solvency of the company.

It also states that in some cases it might be prudent to obtain approval by a shareholders resolution (which can be an ordinary written resolution) approving the transaction. This can reduce or eliminate the risk of a challenge based on breach of duty of the directors, provided there are no insolvency issues.

Solvency Statement in Capital Reductions

The Law Society have published a paper providing guidance on responsibilities under the mechanism introduced on 1 October 2008 enabling capital reductions supported by a Solvency Statement for private companies (Sections 641 to 644 Companies Act 2006). The Solvency Statement has to be signed by all the directors.

Each director has to form the opinions stated in the Solvency Statement and in forming them they must take account of all of the company's liabilities (including any contingent or prospective liabilities). If the directors make a Solvency Statement without having reasonable grounds for the opinions expressed in it they could be liable to imprisonment of up to 2 years and/or a fine. Therefore directors will be expected to exercise reasonable care, skill and diligence in forming these opinions.

Therefore directors are advised to keep a record of the information they considered in reaching their opinion.

The directors will need to identify any facts or circumstances known to them that may affect the company's ability to discharge its debts over the next 12 months. The likely impact of the credit crunch will need to be taken into account, including the likelihood of bank facilities continuing at existing levels or major suppliers or customers ceasing to trade.

There is no requirement in the Act for a report by any third party on the directors conclusions (unlike purchases of own shares out of capital).

In some cases, the directors may wish to obtain advice to reach their opinion or seek comfort on the processes they have gone through (or propose to go through) to help satisfy themselves that their opinion is soundly based. Whether or not the directors decide to do so is likely to depend on their assessment of the difficulties of forming their opinion on the basis of the information they have and the potential benefits of seeking comfort on the processes or taking advice on the things to be taken into account or the reasonableness of any judgements they have to make. Where directors give proper instructions and take account of the advice or comfort received this is likely to be helpful in showing that the directors had reasonable grounds for their opinions. The Company Law Committee of the Law Society believes that if the directors do not obtain a report from an independent third party or advice or comfort on process, this will not necessarily prevent the directors from demonstrating that they had reasonable grounds for the opinions expressed.

The Law Society therefore considers that "comfort on the process" type engagements are sufficient to support the directors' opinion if advice from third parties is needed. If we are asked to advise directors seeking to sign a Solvency Statement we should limit the scope of our work to such a process-based engagement (rather than for example, providing confirmation of the directors' assessment of solvency).

The ICAEW supports this paper because it is important to avoid the possibility of independent accountants reports creeping into banking covenants as a pre-requisite for Solvency Statement capital reductions, as this would be costly and thus would negate the benefits of this important reform.

Arbitration Clauses in Articles of Association

When amending their Articles to take account of Companies Act 2006 matters, some listed companies are incorporating a compulsory arbitration clause in them.

Such clauses are legal, but may not be in the interests of all shareholders because they mean that if shareholders want to sue the company, they are prevented from doing so through the courts and are required, instead, to seek redress through arbitration.

However, the use of such clauses could be useful for private companies with significant minorities whose interests could conflict with those of the other shareholders. The codification of directors duties and the enhanced rights of shareholders to bring derivative actions in the Companies Act 2006, together with the advent of litigation funding, mean that directors and companies are more exposed to legal action, and notwithstanding the fact that any damages awarded only go to the company and not the disaffected shareholders, legal action could become more commonplace which will make such arbitration clauses in the Articles more attractive.

Final Companies Act 2006 Commencement Order

The remaining sections of the 2006 Act will be brought into force from 1 October 2009 under SI 2008/2860 "The Companies Act 2006 (Commencement No. 8, Transitional Provisions and Savings) Order 2008".

Two matters that will be dealt with at this time are:

- ***Restoration of dissolved companies to the Register.*** It has been decided that the time limit, extended to 6 years by the 2006 Act, will apply to companies dissolved on or after 1 October 2007.
- ***Availability of powers to change capital for existing companies.*** All companies, and not just companies formed under the Companies Act 2006, will be able to reduce their capital without Court approval, issue redeemable shares (in relation to private companies only), purchase their own shares, and purchase their own shares out of capital (private companies only) without explicit authorisation in their Articles. They will still need shareholder approval by means of a resolution and the Articles can exclude or restrict the availability of the powers.

ASB issues Amendment on Financial Instruments: Eligible Hedged Items

The Accounting Standards Board (ASB) has issued an amendment to FRS 26 (IAS 39) 'Financial Instruments: Recognition and Measurement – Eligible Hedged Items'. This follows the same amendment issued in July 2008 by the International Accounting Standards Board (IASB).

The amendment clarifies how the existing principles underlying hedge accounting should be applied in two particular situations, namely the designation of one-sided risk in a hedged item, and inflation in a financial hedged item.

The amendment provides additional application guidance to illustrate how the principles underlying hedge accounting should be applied in the above two situations.

Entities are required to apply the amendment retrospectively for accounting periods beginning on or after 1 July 2009, with earlier application permitted. The amendment ensures that FRS 26 remains in line with International Accounting Standard (IAS) 39.

New Independent Examination Guidance for both Charity Trustees and Examiners

New guidance, CC32 "Independent Examination of Charity Accounts: Examiner's Guide" has been published by the Charities Commission. It addresses the changes introduced by the Charities Act 2006 for financial years starting on or after 1 April 2008, in particular, the independent examination of small company charities. CC32 can be downloaded from www.charity-commission.gov.uk

CC32 is designed to provide all the information an Independent Examiner needs to know in order to conduct a competent Examination, including the directions made by the Commission which must be followed. In addition, there is helpful guidance on a range of issues including suggested examination procedures, examiners' reports and on reporting on matters of material significance to the Commission.

The decision whether or not to opt for Examination instead of an audit and the choice of an Independent Examiner are important ones for trustees. The Charity Commission has also produced separate guidance aimed specifically at trustees to help them understand what an Independent Examination involves and what steps they can take to ensure an efficient and effective Examination.

FRC alerts directors to the corporate reporting challenges arising from current economic conditions

The Financial Reporting Council (FRC) recognises that the global liquidity squeeze and its impact on the wider economy increases the challenges for directors of listed and quoted companies in preparing corporate reports this year. This means that more time may need to be spent by the directors and the audit committees in planning the year-end activities, reviewing key assumptions and models used in financial reporting and in reviewing the significant accounting and disclosure judgements.

In response to these challenges, the FRC has published two documents to assist directors by identifying key questions that they may wish to consider when preparing for the year-end and in meeting their responsibilities in relation to annual reports and accounts. These documents do not impose any new requirements on companies or their auditors.

- An analysis of some of the challenges for audit committees arising from current economic conditions and some suggested questions that audit committees may need to address.
- An Update for directors of listed companies on reporting on going concern and liquidity risk.

This Update brings together the key accounting requirements and the disclosures relevant to going concern and liquidity risk and sets out the main points of interaction between the judgements made by directors and auditors. The Update highlights the following challenges for all of the parties involved:

- directors will need to ensure that they prepare thoroughly for their assessment of going concern and make appropriate disclosures;
- auditors will need to ensure that they fully consider going concern assessments and only refer to going concern in their audit reports when appropriate; and
- investors and lenders will need to be prepared to read all of the relevant information in annual reports and accounts before making decisions.

The Update also notes that the absence of confirmations of bank facilities does not of itself necessarily cast significant doubt on a company's ability to continue as a going concern or necessarily require auditors to refer to going concern in their reports.

No responsibility for acting upon or refraining to act upon any item included in the factsheet can be accepted by Bond Partners LLP or the contributor of the item.