

Quarter in law

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Cross-border mergers under the Tenth Directive – update

It has been over a year since the Directive on cross-border mergers of limited liability companies (2005/56/EC) (the Tenth Directive) was implemented in the UK by virtue of The Companies (Cross-Border Mergers) Regulations 2007, which took effect from 15 December 2007.

In the last year, we have seen increasing consideration of cross-border mergers as one of the ways to structure European group operations since the regulations allow UK companies to merge with one or more other European Economic Area (EEA) companies. Several mergers have been registered with UK Companies House in the last 12 months, most, if not all, of them relating to intra-group reorganisations.

Prior to the implementation of the Tenth Directive and the regulations, the nearest equivalent to the merger process in the UK were schemes of arrangement, which are now regulated by the Companies Act 2006. However, there were no provisions in the UK that expressly dealt with cross-border mergers of companies.

The main driver for cross-border mergers has been to simplify group structures to achieve cost savings. This is because the company being merged (the transferor company) will dissolve without being liquidated, and its assets and liabilities will be transferred to the surviving company (the transferee company). From a tax perspective, within the EU any tax charge arising from a cross-border merger will be deferred until the assets transferred to the transferee company are disposed of

(provided that the transferee company has a permanent establishment, for example, a branch) to which these assets are attributable in the relevant Member State. This is the position under the Tax Mergers Directive 90/434/EEC which has been implemented in all Member States as amended by Directive 2005/19/EEC.

A cross-border merger can be achieved by one of the following means:

- by absorption under which one or more transferor companies merges into an existing transferee company;
- by absorption of a wholly-owned subsidiary whereby the subsidiary merges with its parent; or
- two or more transferor companies merging to create a new company.

A merger must be completed in two phases. Firstly, the pre-merger phase whereby (subject to certain exceptions) each individual transferor and transferee company seeks approval of the proposed terms of the merger from their shareholders and demonstrate to their respective national authorities (the courts in the case of the UK) that all the pre-merger requirements have been satisfied. Secondly, in the completion phase, the appropriate authority in the country where the transferee company is incorporated must approve the merger. A director's report must be prepared by all companies involved in the merger explaining the effect of the merger on the shareholders, creditors and employees of the relevant company. An independent expert's report

is also required in certain circumstances. The court also has the power to call for a creditors' meeting to approve the merger.

As at 1 January 2009, the Tenth Directive has not been implemented across the EEA but the table over page shows the EEA countries where the Tenth Directive has been implemented.



Cross-border mergers under the Tenth Directive – update - Cont'd

(Please note, this is only an indicative list and the final position should be confirmed with the individual country.)

Austria	✓	Lithuania	✓
Belgium	X	Luxembourg	✓
Bulgaria	✓	Malta	✓
Cyprus	✓	Netherlands	✓
Czech Republic	✓	Poland	✓
Denmark	✓	Portugal	Permitted under domestic law*
Estonia	✓	Romania	✓
Finland	✓	Slovakia	✓
France	✓	Slovenia	✓
Germany	✓	Spain	Permitted under domestic law*
Greece	X	Sweden	✓
Hungary	✓	UK	✓
Ireland	✓	Iceland (EEA)	Permitted under domestic law*
Italy	✓	Liechtenstein (EEA)	Permitted under domestic law*
Latvia	X	Norway (EEA)	Permitted under domestic law*

* There is domestic legislation to allow mergers independent of the Tenth Directive

Given there is a strict timetable to follow and the courts (or the equivalent authority) need to be involved, it is estimated that completing a cross-border merger will take a minimum of six months. However, this could be longer if there are employee participation negotiations, creditor protection issues or if an independent expert's report is

required. It will also depend on the requirements of the EEA countries of the merging companies as some EEA countries have a lengthier court process than the UK.

Of the issues highlighted above, the most challenging one in implementing a cross-border merger is managing employee rights. The general rule is that the employee participation rights (i.e. the right to be represented in management) under the laws of the country where the transferee company is, will apply. There are exceptions to this general rule, which apply where the participation rights under the local law of the transferee company is lower than those of the merging companies. Potentially it involves the election of a special negotiating body to agree an employee participation agreement between the company and its employees. This will have a significant impact on timing and should be factored in at the early stage of the planning of any structuring projects.

In addition, the choice of the merging companies and where they are incorporated is crucial. As noted above, some of the countries have yet to implement the Tenth Directive by local legislation. While some of these countries have a domestic merger regime, it may not necessarily be compatible with a cross-border merger under the Tenth Directive and it is uncertain whether a merger will be recognised by the other countries which are parties to the merger.

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Regulating retail banking

In November 2008, the Financial Services Authority (FSA) published a consultation paper (CP 08/19) on proposals to regulate the retail banking conduct of business. Under the proposals, the FSA will assume responsibility for regulating conduct of business in relation to retail deposit-taking (other than consumer credit and credit cards, which falls in the remit of the Office of Fair Trading (OFT)). The proposals will apply to firms carrying out the regulated activity of accepting deposits (including related activities such as providing cheques) and issuing e-money to retail investors. In particular, CP 08/19 highlights the importance of issues such as treating customers fairly, transparency of pricing of products and services, provision of information to consumers and post-sale requirements.

The FSA has not previously made comprehensive rules governing the conduct of retail banking business, except where required under EU law. When the FSA was established, its remit did not extend to fully cover deposit taking activities. At that time, the prevailing view was that self-regulation could provide a more cost effective regime where the likelihood of potential market failure was small. The Banking Code and Business Banking Code, which are industry sponsored codes of conduct, contain the current standards of conduct to which firms voluntarily subscribe and adhere. The Banking Code Standards Board (BCSB) monitors adherence to the codes as well as adherence to the FSA's Principles and Conduct of Business Sourcebook (COBS) as it currently applies to retail deposit taking business. The BCSB has disciplinary powers but is not able to impose fines.

After the Payment Services Directive (PSD) takes effect on 1 November 2009, the FSA will become the main competent authority for the PSD conduct of business and other requirements in relation to payment services. The FSA estimates that the PSD will supersede approximately 40% of the provisions in the Banking Code. The FSA has decided to build on the changes required for the PSD and move away from the self-regulation model, to regulate retail consumers' core financial services relationships with banks. The FSA believes that not enforcing Principle 6 (the requirement to treat customers fairly) in this area could leave potential scope for consumer harm. The FSA's changed assessment of the costs benefit analysis of self-regulation also argues for a shift away from the existing model.

Therefore, the FSA is proposing a new framework, to include:

- full application of the FSA's principles to the regulated activities of accepting deposits and issuing e-money;
- introduction of a Banking Conduct of Business Sourcebook (BCOBS), to include retail banking services, primarily relating to the provision of information to customers and post-sale requirements;
- transfer of the FSA's existing conduct of business rules and guidance applicable to deposit taking to BCOBS; and
- the FSA monitoring and enforcing compliance

with the principles and BCOBS. The FSA's current guidance states that in applying the principles to accepting deposits and issuing electronic money it will take enforcement action only in a prudential context. The FSA plans to remove this guidance and enforce the principles in a conduct of business context as well as a prudential context.

The FSA proposes to implement the changes in November 2009 and has indicated that it intends to work closely with stakeholders such as the BCSB, the OFT and sponsors of the codes. The FSA envisages that industry may wish to develop voluntary guidance to support compliance with the new framework perhaps thereby preserving some of the material currently found in the codes.

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Loans to directors – lenders beware!

One of the key changes under the Companies Act 2006 was the removal of the general prohibition on loans by a company to its directors. However, before taking advantage of the relaxation of the rules, it is important to be aware of the details of the Consumer Credit Act.

The change in company law

Under the 1985 Companies Act, companies were prevented from making loans to their directors, directors of their holding company or connected persons unless the loans fell within a specific exception – notably a loan for less than £5,000 or a loan to cover expenses incurred while carrying out the directors' role.

On 1 October 2007, the restriction was lifted so companies could make loans to directors (subject to certain conditions) provided they had the approval of shareholders.

The Consumer Credit Act

The Consumer Credit Act 1974 (the CCA) was originally introduced to redress the balance of power in favour of the consumer and its powers were strengthened in 2006. Its regime for debtor protection has always had the potential to apply to directors' loans but, until the changes in the 2006 Act, this has never needed review. However, the relaxation under the 2006 Act has necessitated a closer look at the CCA.

The CCA applies to the provision of credit to individuals and requires lenders to obtain a licence from the Office of Fair Trading. It is a criminal offence to provide credit to individuals without a licence. Also, credit agreements which are entered into without a licence are unenforceable.

Furthermore, the CCA imposes stringent requirements on the form and content of credit agreements and other matters, making it extremely difficult for most companies who do not do this as part of their normal business.

However, there are some exemptions included within the CCA and, if businesses operate within them, then there is no need for a CCA licence or to comply with the CCA.

Possible exemptions

In the context of directors' loans, the exemptions can be summarised as follows:

- Payment exemption: applies if the loan is repaid by four instalments or less within 12 months.
- Restricted low cost exemption: applies if (i) the loan is offered to a particular class of people (e.g. to directors only) and not to the public generally, and (ii) the interest charged for the credit does not exceed 1% above the base rate of certain UK banks.
- High net worth borrower exemption: applies if (i) the director has a net income of more than £150,000 per annum or net assets exceeding £500,000 (excluding main residence and pension), (ii) an accountant

confirms the income/assets position, and (iii) the loan agreement includes a statement from the director in the prescribed wording agreeing to forgo the protections of the CCA.

These summaries do not include all the relevant details and professional advice should be sought before businesses think about making loans to their directors.

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The impact of the Health and Safety (Offences) Act 2009 on businesses

The issue to have arisen from the Corporate Manslaughter and Homicide Act 2007 which has caused the most concern is the misperception that the Act targets and penalises individuals; specifically those in senior management positions.

The reality is that an individual cannot be liable under the Act or for aiding, abetting, counselling or procuring a commission for the offence of corporate manslaughter (although the theoretical risk of gross negligence manslaughter still exists). Rather, the Act targets organisations.

As a result of the attention that the Act has attracted, a piece of legislation carrying a far greater threat of personal liability from senior management's perspective has slipped under most businesses' radar screens.

The Health and Safety (Offences) Act 2008 which covers Great Britain and Northern Ireland, became law on 16 January 2009. It increases penalties and provides the courts with greater sentencing powers for serious breaches of health and safety legislation.

Under the Act, individuals successfully prosecuted face fines of up to £20,000 in the Magistrates Court for nearly all summary offences and unlimited fines in the Crown

Court. Imprisonment is available for nearly all offences. The Act caters for sentences of up to 12 months in the Magistrate's Court¹. Individuals successfully prosecuted in the Crown Court will face a maximum prison sentence of two years.

Whilst it is still theoretically possible for directors/senior management to be prosecuted individually for gross negligence manslaughter, the effect of the Offences Act is to make it significantly more likely that directors/senior management could face prison or personal fines in respect of their organisation's health and safety failings – especially in the event of a fatality.

A number of commentators believe that the new Act could have affect even for relatively minor health and safety offences. The proof of the pudding will be in the eating, but in instances where there has been a fatality, there does now appear to be a risk of individuals facing prosecution rather than the organisation itself.

As the Department of Work and Pensions Minister, Lord McKenzie, recently put it:

"... These changes will ensure that sentences can now more easily be set at a level to deter businesses that do not take their health and safety management responsibilities seriously and further encourage employers and others to comply with the law. ... Jail sentences for particularly blameworthy health and safety offences committed by individuals, can now be imposed reflecting the severity of such crimes, whereas there were more limited options in the past".

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¹ This apparently is to be read as a reference to 6 months pending the implementation of section 154(1) of the Criminal Justice Act 2003

.tel domain names – the virtual address book

On 3 December 2008, Telnic, a UK based company authorised by the Internet Corporation for Assigned Names and Numbers (ICANN) launched the new top level domain (TLD), .tel, and opened its doors for applicants to register their unique domain name during the early registration period, known as the sunrise period.

The .tel domain name introduces a new way that domain names are used and provides individuals and businesses with a new method of publishing their contact details without creating a website. Existing TLDs are still used as an integral part of the internet domain name address system, such as .com, .org, or .co.uk. However, the new domain name will act as a virtual address book available to any device that can access the internet.

How does it work?

The .tel domain name effectively eliminates the necessity of a website as a medium, allowing faster access to published contact details due to increased processing speeds. When a traditional domain name is entered into a browser, it queries the domain name system (DNS), in which the DNS replies with an IP address. The browser then uses the IP address to locate the website required. In contrast, the .tel domain name has a different purpose and maps domain names to contact information and keywords that the company or individual chooses to store directly in the DNS, such as phone numbers or location maps. The details are then returned directly from the DNS without any re-direction through a

website. This is particularly desirable in the case of mobile phones given the reduction in the quantity of data to be transmitted.

This technology is intended to reduce cost in terms of website maintenance or quantity of data, and it also presents a clear opportunity where internet access is primarily through handheld devices such as a mobile or a smartphone. By using the .tel domain name, the end-user can click on a contact method of choice, such as a phone number, and be connected immediately.

What are the opportunities?

Telnic uses technology which is likely to compete with the traditional yellow and white pages of online address books. The directory nature of the system allows end-users to be guided through vast amounts of information with ease. For example, a larger company could choose to arrange contact details by business unit or location.

The .tel domain name is a big opportunity to increase the ease in which a company can be contacted and has the added benefit of being a live service, where contact details can be updated in real-time.

What are the risks?

Businesses that are registered trade mark owners or authorised licensees of registered trade marks that do not register their own unique .tel domain name, could face the usual risks associated with domain names. Such risks include cyber-squatting or competitors with a similar name registering a similar domain name and

re-directing customers away from their business. This can have an impact on trade mark/brand protection, so registering a .tel domain name within the relevant period could strengthen the protection of the brand.



.tel domain names – the virtual address book - Cont'd

Timetable

Telnic is allowing the purchase of .tel domain names in the following stages:

3 December 2008 to 2 February 2009 at 23:59 GMT

The sunrise period was reserved for the owners or licensees of registered trade marks. Applications were accepted only through ICANN accredited registrars and are subject to a validation procedure operating on a first-come first-served basis. The sunrise registrations carry a three-year minimum term. Trade marks must have been applied for prior to 30 May 2008 and registered prior to the date of application.

3 February 2009 at 15:00 GMT to 23 March 2009 at 23:59 GMT

The landrush period is open to everyone at a premium price and applications can be made through ICANN accredited registrars. The landrush registrations carries a three-year minimum term.

24 March 2009 opens at 15.00 GMT

General availability follows the landrush period and applications will only be accepted through ICANN accredited registrars, and registrations will carry a one-year minimum term.

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