

Companies (Amendment) Bill

Summary of responses received by the Financial Supervision Commission (“the Commission”) to the consultation issued on 21 December 2007 together with the Commission’s response

Glossary of terms:

1931 Act companies = IOM companies registered under the Companies Acts 1931 to 2004

2006 Act companies = IOM companies registered under the Companies Act 2006

CA31 = Companies Act 1931

CA06 = Companies Act 2006

IMF = International Monetary Fund

IOSCO = International Organisation of Securities Commissions

Question 1 (a).

Do you support the proposal to amend the Companies Act 1931 to 2004 (re 1931 Act companies) by –

(a) reducing the period for preparing and laying financial statements before the members for

(i) public companies to 6 months; and

(ii) private companies to 9 months (see 2.4.1. in consultative paper)

Result of consultation

There was general agreement and support for this proposal, however, the contrast with the absence of such obligations on 2006 Act companies was mentioned.

It was also suggested that the IMF’s concerns properly relate to the protection of third party investors and whilst the IOSCO principles seem sensible for quoted and widely held companies, private and closely held companies ought not to be subject to the same rules.

Another respondent suggested that IOM companies whose shares are on the London AIM and other securities markets should be regulated by the rules of those markets rather than by domestic IOM law.

Commission’s response

The draft Bill retains the reduced period of time as mentioned in question 1(a) given the support for the proposal. The period of 9 months for private companies should not prove particularly onerous.

It would not be appropriate for the Isle of Man to relinquish regulation of its own companies on the basis that a market also regulates the company in relation to its listing / registration.

Question 1 (b) introducing a power for the Commission to direct a company to correct a misstatement in its prospectus with such a notice being placed on the company’s public file (see 2.4.3 in consultative paper);

Result of consultation

There was general support for this

Commission’s response

Given the support for this proposal, the

<p>proposal although one respondent said the power should only be used in relation to material errors or misstatements.</p> <p>Another respondent suggested that the absence of a direction on the company's file may be construed as tacit approval of a prospectus. This may lead to defensive submission of a prospectus.</p> <p>It was also suggested that the Commission having "reasonable cause to believe" is too low a standard as it would allow the company concerned to equally have a reasonable view that the statement in the prospectus does not need to be corrected. It was suggested that the standard should be "that there are no reasonable grounds to believe that the statement is true".</p> <p>The respondent also noted that if an investor is dissatisfied, that person would need to seek a remedy through the courts.</p>	<p>draft Bill contains direction powers regarding defective prospectuses.</p> <p>The power is exercisable should the Commission become aware of matters that give it "reasonable cause to believe".</p> <p>The Commission does not consider that the absence of a direction is a tacit approval of a prospectus. The power could be utilised, whether or not a prospectus is submitted, if and when the Commission becomes aware of the untrue or misleading statement. The fact of its being submitted will not prevent the prospectus from being considered after that date in the event that relevant matters are brought to the Commission's attention.</p>
<p>Question 1 (c) placing a general duty on the directors of 1931 Act companies to disclose all material information to investors in relation to an offer to enable them to make informed decisions (see 2.4.4 in consultative paper)</p>	
<p><u>Result of consultation</u> All respondents supported this proposal.</p> <p>In addition, some respondents suggested that the Fourth Schedule to CA31 (<i>matters to be specified in Prospectus and Reports to be set out therein</i>) is antiquated and no longer serves any useful purpose on the basis that the proposed new s.35A will place an overarching duty on the directors to ensure that any prospectus contains all information material to the offer.</p>	<p><u>Commission's response</u> The Commission is persuaded by the argument that the Fourth Schedule to CA31 should be repealed and the draft Bill contains the relevant repealing provisions and consequential amendments.</p>
<p><u>Question 2</u> Do you agree with the proposals to address the conflict between the current statutory accounting/audit requirements and FRS 21 and current best advice on the treatment of dividends in the accounts? If not, please give your reasons and explain how you think this should be addressed</p>	
<p><u>Result of consultation</u></p>	<p><u>Commission's response</u></p>

All respondents supported this proposal.	The support for this proposal is noted.
<p>Question 3</p> <p>Do you agree with the proposals to address the conflict between the current statutory accounting/audit requirements and FRS 25 and, in particular, the proposed new provisions which would allow departure from the statutory requirements, as necessary in order to –</p> <p>(a) give a true and fair view and/or;</p> <p>(b) where accounting standards so require;</p> <p>(c) and the effect of (b) also being to impose an obligation to comply with generally accepted accounting standards; and</p> <p>(d) is the definition of generally accepted accounting standard appropriate?</p>	
<p>Result of consultation</p> <p>All respondents supported (a) and (b) but regarding (c) and (d) several respondents considered the definition of “generally accepted accounting standards” to be too narrowly drawn and suggested it be extended to include US GAAP.</p> <p>Some respondents also recommended that, subject to prior permission from the Commission, other acceptable GAAP’s could be looked at on a case by case basis. This would be determined by the facts of the case. They also commented that it is envisaged that as more jurisdictions use IFRS, the need to consider the quality and appropriateness of other GAAPs is likely to decrease.</p> <p>Two respondents considered that it would be a mistake to specify IASB or ASB standards as in their view this would, in the long term, seriously hamper the Island’s attempts to promote the use of Manx companies in the newly emerging economies, particularly those in Asia, from where IOM is increasingly seeing new business emanate. If accounting standards are to be specified, they suggested that as well as IASB, ASB and US GAAP, other standards considered appropriate by the board of the company, acting on a bona fide and reasonable basis, should also be allowed.</p>	<p>Commission’s response</p> <p>The Commission has extended the definition of “generally accepting accounting standards” in the draft Bill to include US GAAP.</p> <p>A typographical error was highlighted and will be corrected by inserting the word “Financial” - <i>accounting standards and practices recommended by the International Accounting Standards Board (International Financial Reporting Standards) or by the Accounting Standards Board (United Kingdom Accounting Standards).</i></p> <p>The Commission has subsequently consulted with the accountancy professionals in respect of allowing any standard the directors of the company may wish to adopt. This proposal does not appear to meet the requirement to ensure that accounts will be audited to appropriate standards and would undermine the attempt to ensure the quality of audits by specifying particular generally accepted accounting standards. Therefore, as proposed in the draft Bill, any further extension of the definition will be made by regulations under the power for the Commission to specify accounting standards (see new s.17C(2)(c) to be inserted in Companies Act 1982 by clause 19 of the Bill).</p> <p>As discussed with IOMSCA, the Commission intends to seek the advice of the professional accountancy bodies</p>

	<p>on the quality of and equivalence to the permitted accounting standards before making such regulations.</p>
<p>Question 4 Do you agree with the proposal to introduce a regulation-making power to facilitate amendment of accounting / auditing provisions without having to do so by primary legislation which has a very long lead-in time? The intention of such ‘future-proofing’ is so that the Island can react more quickly when there are changes to generally accepted accounting practice, and if needed and it is considered appropriate, to address international pressures for change and to facilitate local circumstances by being so able.</p>	
<p>Result of consultation The proposal was generally supported.</p> <p>Some respondents queried whether the resource and expertise would be available to draft such regulations.</p> <p>One respondent said that prior to the implementation of any proposed regulations, industry should be consulted.</p> <p>It was also queried how it is intended to apply s.17C (2) (h) to (j) in a standard company (non-regulated) environment? Re s.17C (2)(k) the audit report cannot be prepared in isolation and must always be concurrent with the financial statements to which it relates. Any legislation should refer to timeframes for audited financial statements, not the auditors’ report <i>per se</i>.</p>	<p>Commission’s response As would be the case in performing any of its functions, where necessary advice will be sought to supplement the Commission’s in-house expertise.</p> <p>The Financial Services Bill requires the Commission to consult before making any regulations under that Bill and although there is no specific duty to consult in respect of its functions under the Companies Acts, the Commission intends to continue its practice of consulting with those affected before making or recommending that the Treasury makes any secondary legislation under the power contained in the corporate legislation.</p> <p>The powers contained in the new s.17C(2)(h) to (k) of CA82 have been reviewed and will be amended. Power to make regulations affecting <i>the duties of auditors</i> and <i>practices to be adopted by auditors</i> ((h) and (j)) will be retained as in future, for example, to meet international standards it may be necessary to introduce controls in the Island’s domestic law. There is already an implied duty on auditors arising from the directors’ duty to have regard to generally accepted accounting standards (see new s.3A CA82 to be inserted by clause 16 of the Bill).</p> <p>However, as there is potential for (j) (<i>the contents of the auditor’s report</i>) to create conflicts with an auditor’s professional accountancy body’s rules</p>

	<p>and/or GAAPs, paragraph (j) has been deleted.</p> <p>Paragraph (k) has been reworded to refer to the financial statements and not to the auditor's report.</p>
<p>Question 5</p> <p>a) Do you agree with the proposed new approach to auditor qualification, bearing in mind that a change to section 14 CA82 is necessary to allow bodies corporate and unincorporated to act as auditors of Isle of Man companies and that the bye-laws of some of the accountancy professional bodies only recognise individuals and not 'audit firms' as members?</p> <p>b) Is there too much detail including circumstances which are unlikely to ever arise and does it cover the circumstances pertaining in the Island in respect of how audit firms are structured? If any of the circumstances do not apply to the Island or if there are other scenarios which need to be covered please provide the detail of what you suggest should be included in these provisions.</p>	
<p>Result of consultation</p> <p>The proposals were generally supported and the majority of respondents did not consider the detail in the new provisions to be excessive.</p> <p>As the consultative paper remarked that in framing the auditor qualifications English Limited Liability Partnerships had not been specifically considered, some respondents sought clarification regarding the acceptability of English LLPs to qualify as auditors under the new provisions.</p> <p>One respondent advised against the creation of any new Board controlling Manx auditors or audit provisions which differentiate the rules for these bodies from those that have already established international accounting principles.</p> <p>The accountancy professionals suggested that the auditor qualifications in s.14 CA82 was originally premised on IOM law closely following UK & Irish law. The assumption was that UK & Irish professional accounting bodies should therefore have sufficient knowledge of the relevant IOM law. However, as IOM law has now diverged from UK & Irish law, they consider the restriction now to be insufficient.</p>	<p>Commission's response</p> <p>There was no intention to exclude English LLPs from qualifying as auditors, simply to make specific provisions for Isle of Man persons. The Commission is now aware as a result of the consultation that there is a need to clarify that such structures qualify as auditors. The drafting of the new s.14B CA82 which sets out the requirements for a body corporate also would apply to English LLPs which are bodies corporate. It is not therefore proposed to make any change in this respect as English LLPs would qualify provided they meet the requirements of the new s.14B CA82.</p> <p>There is no intention to create an IOM 'Board' to control auditors but regulations may be needed in the future. For example, if other security markets introduce audit rules as is the case with the EU Directive on Statutory Audits.</p> <p>The arguments on both sides relating to whether or not to limit auditors to those resident on the Island were persuasive. Ultimately the Commission considered its objectives and the factors that it is statutorily obliged to consider when meeting these objectives. It was decided that the objectives were best met by recognising the increasingly global use to</p>

<p>They also pointed out that with a wider global reach of some of the qualifications, a variety of overseas individuals can sign IOM company audit reports without any experience of IOM law. Professional standards vary from country to country and standards of corporate governance which may be the norm in many countries would not be acceptable in the IOM. They therefore suggested adding an IOM residential qualification to ensure the requisite knowledge of local law and regulations.</p> <p>Other respondents took the opposite view citing the example of AIM companies with 'foreign' auditors where investors are content to invest in, for example, an AIM company knowing that it has foreign auditors. These respondents considered it better for the audit to be conducted by an auditor who is based in and familiar with the entity's business in its key jurisdictions of operation rather than in its jurisdiction of domicile where it may have little, if any, operations on the ground. An IOM residence requirement would only add another layer of cost without necessarily adding value and would, in their view, make IOM companies less attractive.</p>	<p>which Isle of Man companies are used, and that there will be occasion when the appointment of auditors outside of the Island, the UK or Ireland may be appropriate. Therefore the draft Bill contains a provision to allow the Commission to authorise other auditors in appropriate circumstances.</p>
<p><u>Question 6</u> Do you have any comments on the proposal to introduce a specific regulation-making power to allow Manx auditors to continue to audit companies which are admitted to trading on the regulated markets of EU Member States and the extension of this to 2006 Act companies?</p>	
<p><u>Result of consultation</u> There was general support for this proposal.</p> <p>One respondent remarked that the principle sounds sensible but they would like to know more about how this procedure will actually operate.</p>	<p><u>Commission's response</u> In co-operation with Jersey and Guernsey, further discussions to put in place audit monitoring and oversight equivalent to those in and acceptable to EU Member States, have further clarified what regulations will be needed for the Isle of Man to achieve Third Country 'equivalence' in compliance with the EU 8th Directive on Statutory Audits. The regulation-making powers have been widened accordingly and are no longer</p>

	<p>restricted by specifying the EU only.</p> <p>The Commission will consult before making any regulations which may be needed in the future to ensure access for IOM companies to global financial markets.</p>
<p>Question 7</p> <p>Do you have any comments on the proposed amendments to the ‘accounting records’ provisions in CA06?</p> <p>If you disagree with the proposed approach, please explain how you would suggest the Isle of Man could meet its international obligations to cooperate in the reduction of financial crime if a 2006 Act company’s accounting records are not held in the Isle of Man or if held off-Island, they cannot be accessed in a timely manner in the Island?</p>	
<p>Result of consultation</p> <p>Some respondents, including two representative associations, supported the proposal. Others, including two representative associations, opposed it but for different reasons.</p> <p>On the one hand, some feared that the proposals may make IOM companies commercially unacceptable and economically unattractive. They suggested that the onus should be on the directors of a 2006 Act company to operate in the manner that they see fit but with a mandatory obligation to supply accounting records upon specific request (within 28 days).</p> <p>Others suggested that because it is unclear what comprises ‘accounting records’, the proposals were flawed as a mechanism for enforcing access to the records in the case of dispute or fraudulent activity. Instead they proposed that access be made a mandatory condition of the terms of business of the registered agent.</p> <p>In respect of good corporate governance, 2006 Act companies should be required to prepare financial statements, with an option for an abbreviated form in certain circumstances. They argued that directors use financial statements as their primary tool to monitor a company’s</p>	<p>Commission’s response</p> <p>The divergent views reflect the difficulties arising from CA06 currently not requiring the preparation of financial statements.</p> <p>Whilst it is not proposed to make the preparation of financial statements mandatory nor to prescribe in any detail how such statements must be prepared, the principles of ‘true and fair view’ and compliance with generally accepted accounting standards will remain as in the draft Bill. Also, to ensure that any financial statements prepared are of sufficient quality, if audited, the qualification for auditors will apply.</p> <p>However, where financial statements are available, there will no longer be an automatic right for members to be able to access the accounting records but directors and the authorities will continue to have the right to access those prime records.</p> <p>In response to consultation comments, the requirement (where accounting records are not held by the registered agent) periodically to provide the registered agent with copies of accounting records, has been reduced from 6 monthly to 12 monthly.</p> <p>It is important that this provision is retained in order for the Isle of Man to</p>

affairs and do not normally request to see the entries in the prime books of entry although they must be able to access the prime records if they wish to make detailed enquiries.

Other respondents, however, suggested the very essence of the provisions in the 2006 Act were for much more flexibility to be allowed and it would be a retrograde step to force for all 2006 Act companies into producing such prescribed statements.

Some respondents considered the proposed requirement for accounting records to be sent to the registered agent at least every six months too onerous and impractical.

Some respondents noted that it is a widely accepted principle that companies prepare financial statements once only during a financial year and it is not expected that in the interim, a company's financial records be regularly updated and made available to third parties.

meet its international obligations.

Question 8

Bearing in mind the accountancy profession's concerns that the lack of accounting and auditing rules in the Companies Act 2006 may pose a reputation risk for the Island, do you agree that these minimal 'rules' are appropriate to the circumstances in which a 2006 Act company is obliged to prepare audited accounts which may have wider publication than the accounts of a private company and therefore be open to scrutiny?

If not, please give your reasons and any alternative suggestions.

Result of consultation

Whilst the majority of respondents supported the proposal there were divergent views on the proposal that the audit of a 2006 Act company should be conducted by an auditor meeting the same qualifications as those for an auditor of a 1931 Act company.

Commission's response

The draft Bill continues to require an auditor of a 2006 Act company to meet the requirements of auditors of 1931 Act companies.

However, as noted above, the Commission has a power to authorise an auditor for a company that falls outside these requirements in appropriate circumstances, thus recognising the international nature of Isle of Man companies.

	(See also the Commission’s response to consultation comments in respect of question 7 above.)
<p><u>Question 9</u> Do you have any comments on the proposal to – (a) Remove the requirement for a 1931 Act company to file a statement in lieu of prospectus? If not, please give your reasons and any alternative suggestions. (b) Clarify that the registration of charges only applies to charges over property which is beneficially owned by the company? If not, please give your reasons and any alternative suggestions.</p>	
<p><u>Result of consultation</u> All respondents supported these proposals. One respondent requested that the expression “beneficial ownership” be defined.</p>	<p><u>Commission’s response</u> The support is noted. Additionally the wording of the Bill has been further clarified to better provide for complex security cases.</p>
<p><u>Question 10</u> Bearing in mind that the proposed substitution relating to the giving of financial assistance for the acquisition of shares follows the example in the new English Companies Act 2006 (sections 677 to 683), you are asked to consider if – (a) this is desirable; and, (b) whether you consider the risk referred to in 5.4.3 above is likely and if so, whether it would be adequately addressed if it is possible to include a saving provision in the commencement order? In particular, those who suggested this change should consider carefully whether it achieves what they desired and if not, suggest what revisions they consider necessary.</p>	
<p><u>Result of consultation</u> General agreement was evident but it has been suggested that the prohibition on public companies should be removed. This would go further than the UK’s Companies Act 2006.</p>	<p><u>Commission’s response</u> The support is noted, as is the request to go further than this and remove the prohibition public companies. However, the Commission would like to properly consider this suggestion and consult upon it in due course. Therefore the draft Bill has not been amended at this stage, but the Commission will consider the suggestion in due course and seek necessary legislative amendments in the future if required.</p>
<p><u>Question 11</u> Do you have any comments on the proposed amendment to the Limited Liabilities Companies Act 1996 which will remove the automatic default to winding up if no notice of the intention to continue the LLC is filed on the death or resignation of one of the members?</p>	

<p><u>Result of consultation</u> There was general agreement with this proposal.</p>	<p><u>Commission's response</u> The agreement is noted.</p>
<p><u>Question 12</u> Do you have any objection to the addition of Singapore registered Public Accountants who audit companies with securities listed on the Singapore Stock Exchange (which has stringent rules regarding financial disclosures) by amendment to the current s.14 CA82? The Bill will in due course substitute new auditor qualification provisions including a power for the Commission to authorise other auditors who do not meet the qualification criteria, on a case by case basis.</p>	
<p><u>Result of consultation</u> This question was raised by the Commission for a specific purpose and related to the period between the present time and the coming into force of the draft Bill. Respondents queried why Singapore is particular?</p>	<p><u>Commission's response</u> The Commission has determined not to make such a change to s.14 CA82 in this interim period, as the timescale for the draft Bill and the powers contained within it are insufficient.</p>
<p><u>Question 13</u> Comments are invited on this proposal which is aimed at ensuring that the transparency in respect of significant matters in the affairs of a 1931 Act company should extend to a unanimous resolution to dispense with the audit of its financial statements. The form of the amendment to the Audit Exemption Regulations 2007 has not yet been decided but we are taking this opportunity to gauge opinion on the proposal.</p>	
<p><u>Result of consultation</u> Respondents pointed out that as accounts of Isle of Man companies are not made available to the public, there is no need for the dispensing of their audit to be a public matter.</p>	<p><u>Commission's response</u> The Commission is persuaded by the response, and the filing of such a resolution will not be made mandatory.</p>
<p><u>ADDITIONAL COMMENTS</u></p>	
<p>One respondent suggested that the Companies Acts 1986 be amended to bring 1931 Act companies into line with the 2006 Act companies by allowing a company to put restrictions on its activities into its memorandum.</p>	<p>This matter has not been taken forward at the present time.</p>
<p><u>Certificates of Good Standing</u> It was noted that the Companies Act 2006 specifies what must be contained in a Certificate of Good Standing issued by the Registrar. However as voluntary filing of the registers of directors and members is permitted, one respondent requested the content of Certificates of Good Standing be extended to cover</p>	<p>The Registrar will, on request, supply a certified copy of any documents filed including those filed voluntarily and the Commission does not therefore consider this to be an issue.</p>

such information.	
<p><u>2006 Act companies limited by guarantee and having a share capital (a hybrid company)</u></p> <p>One respondent complained about the provisions which require a shareholder of a 2006 Act hybrid company also to be guarantors.</p>	<p>This matter is not at the Commission's insistence, and is a drafting issue. No change is being made at the present time.</p>
<p><u>Employee Share Schemes and Offers to the Public</u></p> <p>One respondent noted that there are several legislative provisions designed to encourage the establishment of employee share schemes by companies. However, s.342(4) (b) CA31 provides that an offer or invitation is not to be construed as made to the public by the company concerned by reason only that it is made "to existing or former employees of that company". Therefore, an employee share scheme made available by a company to employees of other companies within the same group could be construed as an offer to the public.</p>	<p>The Commission agrees with the suggested change, which is now in the draft Bill.</p>
<p><u>Treasury Shares</u></p> <p>Some respondents suggested that it would be very beneficial for the Isle of Man to introduce treasury shares, in particular in relation to listed companies.</p> <p>The law was amended in the United Kingdom to permit treasury shares by the Companies (Acquisition of Own Shares) (Treasury Shares) Regulations 2003 which were under s.2(2) of the European Communities Act 1972 (of Parliament) following a consultation process. Equivalent provisions are carried through to the UK's new Companies Act 2006).</p>	<p>The Commission has considered this suggestion and the draft Bill now contains regulation making powers regarding treasury shares.</p> <p>Before making any regulations we will properly consider this suggestion further and consult upon it in due course.</p>