

Are your company's articles fit for purpose?



Most companies in the UK are set up using the model articles of Association, which are a ready-made set of governance rules for a company. Many founders don't give much thought to whether model articles are appropriate for their business. However, there are several reasons why model articles might not always be suitable for your company, from the outset and as your business grows.

A quick re-cap: what are articles?

Articles of association – usually abbreviated to just “articles” – are written rules governing the operation of a company, as agreed upon by its shareholders. Articles are required for every company incorporated under the Companies Act 2006 (**2006 Act**) and must be produced and made available for public viewing at Companies House when a company is registered.

What are model articles and why were they introduced?

Model articles are a default set of articles which will apply automatically to your company from formation unless you provide amended (bespoke) articles. The model articles were introduced with the aim of simplifying matters for businesses, by providing standard articles suitable for most SMEs without the need for extensive legal input.

There are different model articles for different legal forms of company, including private companies limited by shares, private companies limited by guarantee and public companies. This blog post looks at the model articles for private companies limited by shares, as this is by far the most common type of company operating in the UK.



Why might the model articles not be suitable for your company?

Although the model articles aim to simplify things for smaller businesses, some companies may benefit from alternative provisions and/or more flexibility in certain areas.

1. **Model article 11(2): directors' meetings**

The quorum (number of directors needed) for a valid board meeting under the model articles is two directors. For smaller companies which may only have only two directors, this might delay decision-making if both directors are unavailable. Quorum requirements can also be problematic because the model articles prevent a director from counting towards the quorum if they have an interest in the matter being considered (see model article 14 below). Additionally, recent case law has introduced uncertainty about whether a company with unamended model articles can legally function with just one director.

We recommend amending the model articles to provide flexibility and certainty in such circumstances.

2. **Model article 14: directors' conflicts**

Model article 14 prevents a director from voting on a proposal (and counting in the quorum for a vote on that proposal) if they are personally interested in that proposal.

This model article is aimed at protecting shareholders against directors potentially taking their own interests into account rather than those of the company's shareholders when making decisions on certain matters. But in smaller companies, where the directors are often also the shareholders, this model article can often result in unnecessary delays and/or paperwork because directors need to obtain formal shareholder approval before they can approve such matters.

If this is the case, we recommend amending the model articles to allow directors to participate in decision-making on matters in which they are interested.

3. **Model article 18: removing directors**

Removing non-performing directors can be a challenge under the model articles. We recommend amending model article 18 to make it easier for shareholders or other directors to remove a director who is not contributing effectively to the business.

4. **Model article 21: fully paid-up shares**

Companies with model articles can only issue shares which are fully paid up. Accordingly, companies wishing to issue part or nil-paid shares, which we commonly encounter when helping clients set up employee share schemes, will need to amend model article 21 to include bespoke drafting to ensure the company has the right to call for full payment when required.



Model article 22: share issues

This model article gives shareholders the power to create different classes of shares (e.g. shares with different voting or dividend entitlements such as preference shares). However, many companies might prefer to grant such power to the directors (within certain parameters). If this is the case, the model articles should be amended to allow for this flexibility.

6. Pre-emption rights

The 2006 Act provides that, on any issue of new shares, existing shareholders are first afforded the right to be offered those new shares in proportion to their existing shareholdings. These are called 'pre-emption rights'. In practice, companies rarely want to make a pre-emptive offer for a variety of reasons – the time it takes, the extra admin, the lack of flexibility in the terms of the offer. If this is the preference, then the model articles can be amended so as to disapply these statutory pre-emption rights.

7. Share transfers

There are no restrictions in the 2006 Act or the model articles which would prevent an existing shareholder transferring their shares. Shareholders are therefore free to sell their shares to anyone else – inside or outside the company – at whatever price they choose. In private companies, where the identity of the shareholders is often key, the existing shareholders may prefer to include some form of restriction on share transfers in the articles (including dealing with the situation where a shareholder dies). We can assist with the drafting of such provisions, which often requires careful thought and consideration of the position of individual shareholders.

How can Cripps help?

Taking the time to customise your articles now can save time, reduce costs, and help prevent potential issues down the line as your business grows and evolves. Whether you're setting up a new company or your business is growing and the ownership structure is changing, bespoke articles are worth investing in. Where multiple shareholders are engaged with the business, consider also drawing up a shareholders' agreement, which can add an extra layer of protection for key stakeholders and provide a governance structure for more of the day-to-day business needs of a company.

Reach out to us for expert advice on creating articles as well as on establishing a corporate governance structure that supports your vision and business goals over the long-term.



[Victoria Baxter](#)

Paralegal Apprentice



[Beth Barns-Graham](#)

Managing Associate