DRAFT COMPANIES (AMENDMENT No. 5) (JERSEY) LAW 199

Lodged au Greffe on 22nd September 1998
by the Finance and Economics Committee

STATES OF JERSEY

STATES GREFFE

175 1998 P.195

Price code: B

REPORT

IMPACT OF EMU - REDENOMINATION OF SHARE CAPITAL

Companies incorporated under the Companies (Jersey) Law 1991 often have their share capital denominated in the currency of any number of different countries in the world. Jersey faces a number of issues in preparing for the redenomination of the share capital of such companies as a result of European Monetary Union. These have been investigated, both in the context of companies with share capital in currencies which will be participating in European Monetary Union ("EMU") on 1st January 1999 (the "in-currencies") and Sterling, which is currently not participating. Described below are the areas giving rise to the draft Companies (Amendment No. 5) (Jersey) Law 199 .

The issues needed to be considered in respect of the following periods -

(a) in respect of companies with share capital in Sterling, between the start of the third stage of EMU (1st January 1999) and the date when the United Kingdom joins EMU. It should be noted that (setting aside the larger political question of whether Sterling will ever join EMU) the mechanisms whereby Sterling may join EMU have not yet been determined. It is widely thought that a transitional period shorter than three years will be used, and it also does not necessarily follow that the other aspects of the Transitional Period (for example the parallel existence of "euro units" and "national currency units" as sub-divisions of the euro) will necessarily apply as is planned for the first wave countries. The premise must be for the moment that a similar mechanism will be followed in relation to Sterling when it joins EMU;

(b) in respect of companies with share capital in an in-currency, during the Transitional Period and at the end of the Transitional Period. The steps which are necessary in relation to the Transitional Period will, therefore, so far as they apply to companies which have their share capital denominated in an in-currency, need to be in place earlier rather than later and preferably by early 1999.

The main issues summarized below are -

(1) whether specific legislation is required to permit conversion and/or redenomination of share capital;

(2) rounding issues, and in particular the level at which share capital is to be rounded upon conversion/redenomination;

(3) what changes, if any, need to be made to company procedures to facilitate the conversion/redenomination to euros; and

(4) action in relation to share certificates.

The two pieces of European legislation which are relevant are Council Regulation (EC) No. 1103/97 of July 1997 (the "First Regulation") and Council Regulation (EC) No. 974/98 of May 1998 (the "Second Regulation").

1. Specific legislation to permit conversion/redenomination of share capital

(i) Share capital denominated in Sterling

While Sterling remains out of EMU, the euro will exist in the same manner as any other foreign currency and companies may use the provisions of Article 38(1)(e) of the Companies (Jersey) Law 1991 (the "1991 Law") allowing currency conversion by special resolution. Article 38(3) already specifies a 30-day period during which the conversion rate may be determined, which should be a satisfactory balance between giving sufficient time to assess the precise nominal amounts of the resulting par values, and ensuring that the conversion takes place at the shares' "real" value on the conversion date.

(ii) Share capital denominated in an in-currency

(a) *Transitional Period*

On 1st January 1999 the share capital of all Jersey companies denominated in an in-currency will be automatically converted (without recourse to Article 38(1)(e) of the 1991 Jersey Law) to the euro, but will continue to be denominated in the relevant in-currency (as a "national currency unit" of the euro). Companies may wish to redenominate their share capital from an in-currency to a euro unit. As Article 38(1)(e) refers only to *conversion to another currency*, it is essential, based on a strictly literal reading of Article 38(1)(e), that a provision specifically permitting a new *denomination* (i.e. a conversion to a different unit of the same currency) of share capital into euro units during the Transitional Period be included in the Companies Law. This will be achieved by Article 1 of the Amendment Law.

(b) *End of Transitional Period*

European legislation - and therefore the laws of the Member States participating in EMU - provides that from 1st January 2002 onwards, all references to the in-currencies shall be read as references to the euro according to the fixed conversion rate. Thus, redenomination of the share capital of Jersey companies in an in-currency will effectively occur automatically by operation of law and will be recognised by Jersey law (pursuant to the *lex monetae* principle).

2. **Rounding and level of conversion**

(i) Share capital denominated in Sterling

There is no prescribed degree of accuracy of the conversion rate which would apply to Sterling/euro conversions prior to Sterling joining EMU, nor any proposals that there should be one. Given that the conversion rate will in any case be floating at this stage, and companies would have a choice of 30 days prior to conversion on which the rate could be fixed, it would seem to be an unnecessary and somewhat illogical restriction to impose a prescribed accuracy of the conversion rate.

Article 38(1)(e) of the 1991 Law leaves the principal "rounding" question - the level at which conversion of share capital takes place - open, giving companies the maximum flexibility in converting to the euro. It is believed that this is the correct framework, and it does not seem to be desirable to impose uniformity on how rounding should occur in respect of Sterling while it remains outside EMU.

(ii) Share capital denominated in an in-currency

(a) *Transitional Period*

During the Transitional Period, redenomination between units of the relevant in-currency and euro units shall be carried out using the prescribed conversion rate, which is fixed in the Second Regulation. The prescribed accuracy (six significant figures) of the conversion rate and the way in which it may be used is contained in the First Regulation. These will become part of the *lex monetae* of the Member State of the currency in question and therefore should be recognised by the Jersey courts.

The First Regulation also deals with rounding during the Transitional Period. It appears to provide that rounding need only occur when a monetary amount is to be "paid or accounted for".

The total amount of the *issued* share capital is an amount to be accounted for; it is less clear however whether the *authorized* share capital is also an amount to be accounted for. The question whether the *par value of individual shares* is an amount to be paid or accounted for has been the subject of much discussion in Member States and at the level of the Commission, particularly as the conversion and rounding of the nominal value of individual shares and of the total share capital is likely to result in the sum of the nominal value of individual shares differing from the value of the total share capital.

The Commission has recently suggested that the First Regulation "does not require that individual shares which are redenominated will have to be rounded". It suggests further that "even though the nominal value of a share qualifies as a monetary amount to be accounted for in the sense of [the First Regulation], rounding such amounts after a conversion to the nearest cent only has to be understood as a minimum standard of accuracy. Therefore, companies can decide not to round the nominal value of the redenominated individual shares and thereby ensure that no mismatch occurs between the sum of the redenominated shares and the value of the total share capital expressed in the euro unit. Such a mismatch could conflict with Community company law, which prohibits that the sum of the nominal value of individual shares exceeds the total share capital".

Therefore, assuming that this interpretation by the Commission is not overruled, no Jersey legislation is required to deal with the inconsistencies which would arise if rounding were required at both levels.

(b) *End of Transitional Period*

As noted above, redenomination of share capital in an in-currency will occur automatically on 1st January 2002, in the sense that references to the relevant in-currency shall be "read as" references to euros.

The language of the Second Regulation, which deals with the end of the Transitional Period, suggests that the same rounding rules as in the First Regulation apply, which would mean that rounding happens in the same instances as during the Transitional Period. The Commission has adopted the same approach in clarifying rounding issues at the end of the Transitional Period as during it.

3. **Capital Alteration Processes - resolutions and court orders**

(i) Share capital denominated in Sterling

The present Article 38(1)(e) procedure (conversion of share capital from one currency to another) involves a Special Resolution (two-thirds of shareholders); it is felt that this procedure is adequate and appropriate.

However, it is now proposed that an amendment be made to Article 61 of the 1991 Law (Special Resolution for reduction of share capital) removing the need for a court order if the conversion and consequent rounding results (in itself) in a reduction of capital and so long as the amount of any such reduction is credited to a capital account. This is the effect of Article 3 of the Amendment Law.

(ii) Share capital denominated in an in-currency

(a) *Transitional Period*

In this case, ultimate redenomination into euro will have become inevitable, the mechanisms for such redenomination will be fixed (see above) and the freedom of the company and its members will effectively be restricted to choosing the timing of the final redenomination.

Consideration has been given to a different approval process (such as providing for an ordinary resolution of shareholders or a resolution of the board of directors to approve redenomination) but the view is that a special resolution of shareholders should be retained as the mechanism of corporate authorization.

Where such redenomination in itself results in a reduction in capital, it is considered that Jersey legislation should provide that a court order approving such reduction is not necessary, as long as such reduction is credited to a capital account, and this will also be achieved by Article 3 of the draft Amendment Law.

(b) *End of Transitional Period*

Redenomination into euro units will occur automatically by operation of law, without any corporate approval procedure or need for any court order.

4. **Share certificates**

The question has arisen as to whether a company would be required to issue new share certificates upon conversion to the euro. This would impose a significant administrative burden on companies and would produce particularly ungainly share certificates. It is not a requirement of Article 50 of the 1991 Law for companies to include the par value on a share certificate and there should therefore be no necessity for new share certificates to be issued upon a simple redenomination. It is believed however that it would be helpful to have this point confirmed in Jersey legislation and this will be achieved by Article 2 of the draft Amendment Law.

5. **General**

These are complex matters and it is confirmed that all relevant professional and other bodies have been consulted about the changes.

Explanatory Note

This draft Law, which would further amend the Companies (Jersey) Law 1991, has the following effect.

Article 1 enables a company whose issued or unissued shares are converted into another currency, but remain denominated in the former currency, to change their denomination accordingly by altering its memorandum of association by special resolution.

Article 2 provides that a share certificate continues to be *prima facie* evidence of title to shares, notwithstanding any subsequent change in the currency of the shares to which the certificate relates.

Article 3 enables a company to reduce its share capital, without having to obtain the confirmation of the Royal Court, if the reduction does not reduce liability on unpaid shares, or the net assets of the company, and the amount of the reduction is held in a capital redemption reserve that is used only in paying up unissued shares as fully paid bonus shares.

Article 4 provides that this amending Law will come into force on the seventh day following its registration in the Royal Court.

COMPANIES (AMENDMENT No. 5) (JERSEY) LAW 199

A LAW to amend further the Companies (Jersey) Law 1991, sanctioned by Order of Her Majesty in Council of the

(Registered on the day of 199)

STATES OF JERSEY

The day of 199

THE STATES, subject to the sanction of Her Most Excellent Majesty in Council, have adopted the following Law -

ARTICLE 1

(1) In paragraph (1) of Article 38 of the Companies (Jersey) Law 1991,[1] as amended (hereinafter referred to as "the principal Law") -

(a) for the word "; and" in sub-paragraph (e) there shall be substituted a semicolon;

(b) after sub-paragraph (e) there shall be inserted the following sub-paragraph -

"(ea) in the case to which paragraph (1A) refers, denominate the nominal amount of its issued or unissued shares in units of the currency into which they have been converted;".

[1] Volume 1990-1991, page 916.

(2) After paragraph (1) of Article 38 of the principal Law there shall be inserted the following paragraph -

"(1A) Sub-paragraph (ea) of paragraph (1) refers to the case in which -

(a) the nominal amount of the shares concerned is expressed in one currency;

(b) those shares are then converted (whether under sub-paragraph (e) of that paragraph or otherwise) into shares of a nominal amount of another currency; and

(c) they nevertheless remain denominated in the former currency.".

ARTICLE 2

(1) For the word "A" in Article 51 of the principal Law[2] there shall be substituted the words "(1) A".

(2) After paragraph (1) of Article 51 of the principal Law (as amended by paragraph (1) of this Article) there shall be inserted the following paragraph -

"(2) Paragraph (1) applies notwithstanding any subsequent change of the currency in which the nominal amount of the shares to which the certificate relates is expressed.".

ARTICLE 3

After paragraph (2) of Article 61 of the principal Law[3] there shall be inserted the following paragraph -

"(2A) Notwithstanding paragraph (1), a reduction of share capital shall not be subject to confirmation by the court if -

[2] Volume 1990-1991, page 927.
[3] Volume 1990-1991, page 938.

(a) the reduction does not extinguish or reduce the liability on any share in respect of capital which is not paid up; and

(b) the reduction does not reduce the net assets of the company,

and the amount of the reduction is credited to a capital redemption reserve which may be applied only in paying up unissued shares which are to be allotted to members as fully paid bonus shares.".

ARTICLE 4

This Law may be cited as the Companies (Amendment No. 5) (Jersey) Law 199   and shall come into force on the seventh day following its registration.