

From 'housekeeping' to 'gatekeeping': the enhanced role of the company secretary in the governance system*

Abstract

The role of the company secretary has been transformed from that of chief administrator of a company to corporate gatekeeper. This transformation has been driven by the increasing importance of capital markets which require transparency and board independence to ensure investor confidence. The attribute of independence is critical to performing the function of corporate gatekeeper by being chief of staff to the chairman and in managing the law and policy compliance programme within a group of companies. The independence of the company secretary is best maintained by a professional code that provides negative criteria. In the event of dismissal, a company secretary should have the right of representation to the board with disclosure in the annual report. While professional services firms, as external services providers, can supply needed expertise, the attribute of independence should be regulated through disclosure of potential conflicts and obtaining shareholder approval. The law should further clarify the rules of attribution to avoid unintended consequences. Finally, confidentiality protection should be given to communications with the company secretary to encourage the use of the office by board members for advice on governance.

Introduction

The company secretary is an English corporate invention and the office has continued to this day to enhance transparency and facilitate board independence. The removal of the requirement to appoint a company secretary to a private company by the Companies Act 2006 creates an opportunity to have a sharper focus on this 108-year-old corporate office with increased corporate governance duties.¹ This English invention of a corporate officer has only been exported in a limited way, notably to other common law jurisdictions such as Hong Kong and Singapore. China, as a civil law country, has also installed this statutory officer in their company structure. Despite the legal installation of this office, the company secretary's function as a corporate gatekeeper has not been discussed as extensively as other gatekeepers such as auditors, compliance officers and lawyers,² either in the UK or at any transnational level such as the EU or OECD. The aim of this paper is to explore how the company secretary, as a

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¹ CA2006, s 270; Although the background thinking is under the motto of 'think small first' to reduce red tape for small companies, it has the effect of placing more emphasis on the public companies' governance. See DTI Company Law Reform White Paper (2005), section 4.

² In some countries, public regulators also perform a significant role as corporate gatekeeper. In this sense, the corporate professionals are the private corporate gatekeepers. David Freeman Engstrom 'Agencies as litigation gatekeepers' (2013) 123(3) Yale Law Journal 616. Julia Black 'Entrolling actors in regulatory systems: examples from UK financial services regulation' (2003) Public Law 63-91.

corporate professional,³ can perform an oversight function to increase the impact on the quality of governance. To this end, the paper will argue that a company secretary can act as a corporate gatekeeper who is in charge of facilitating investor-led corporate governance built on transparency and board independence. This role can be fulfilled by professional services firms that have been providing corporate gatekeeper services since the advent of capital markets. At the transnational level, the company secretaries of multinational companies have the potential to shape new transnational governance since they manage increasing numbers of joint law enforcement actions. The change of the role of the company secretary can also have consequences to the quality of the system of governance. EU and other transnational regulators should not overlook the ability of a company secretary, as a corporate gatekeeper in addition to regulators and other corporate professionals, to close gaps in governance.

There are four parts to this paper. In part I, the author will examine the evolving role of the company secretary from a mere servant to a corporate governance officer, and how this office continues to evolve in an investor-led corporate ecosystem where investor communication has become the cornerstone of governance. In part II, consideration will be given to whether the company secretary should also be an officer with independence equivalent to that of auditors, lawyers, and compliance officers. If so, how can such independence best realise corporate values and how can it be regulated? In part III, an investigation will be made into how professional services firms, especially those who provide multiple corporate services, can play a role in adding value to the system of governance and how independence can be maintained in the face of market competition. The way in which a company secretary's liability may be attributable to the professional services firms will be investigated in order to identify any areas that need particular legislative attention to avoid any confusing interpretation of the current law. In part IV, the author will explore the role of the company secretary in the transnational context and discuss what the advantages and disadvantages are of combining the role of company secretary with that of the general counsel office in multinational groups of companies.

Part I The evolving role of the company secretary

In this part, the author will give an account of how the role of the company secretary evolves with investor-led governance. The company secretary is an officer of the company and has served an important role in the administration and management of the company's affairs.⁴ The role has changed from a mere servant of the company to a statutory officer who assumes managerial functions

³ Other corporate professionals are auditors, corporate lawyers, and compliance officers. J Coffee *Gatekeepers. The role of the professions in corporate governance* (OUP Oxford 2006). R Kraakman 'Gatekeepers: The anatomy of a third-party enforcement strategy' (1986) 2 *Journal of Law Economics and Organization* 53-104; Dalvinder Singh 'Role of external auditors in bank supervision: A supervisory gatekeeper' (2013) 47(1) *The International Lawyer* 65-98.

⁴ *Panorama Developments (Guildford) Ltd v Fidelis Furnishing Fabrics Ltd* [1971] 2 QB 711 (CA).

such as chief of staff to the chairman or advisor to the board. The role of company secretary has a shorter history than that of corporate auditor - another corporate gatekeeper. The UK did not include the company secretary in the Companies Act 1855 where the principle of limited liability was first introduced.⁵ In *Barnett, Hoares and Co v South London Tramways Co*,⁶ immediately after the principle of limited liability was introduced in that Act, Lord Esher M.R. said 'A secretary is a mere servant; his position is that he is to do what he is told, and no person can assume that he has any authority to represent anything at all...'. It is important to note that there was no legal requirement in 1887 to have a company secretary which is why Lord Esher thought that this non-statutory role was a mere servant. The company secretary did not receive an official title until the early 1900s when British stock exchanges were becoming more international and offered British companies' shares abroad⁷. The Companies Act 1908 required each company to appoint a company secretary, while the Companies Act 1929 subsequently prescribed the duties and responsibilities of the office. The creation of such a statutory corporate officer has led to the judicial recognition of the company secretary with the authority, usually only conferred on directors, to bind the company with third parties. In *Panorama Developments (Guildford) Ltd. v Fidelis Furnishing Fabrics Ltd*,⁸ the court recognised the company secretary as an officer of the company having authority to bind the company with third parties. In the same case, Salmon L.J. described a company secretary as the chief administrative officer of the company but left open the question whether he would have any authority in relation to the commercial management of the company. Since then, the emphasis on the function of the company secretary has shifted to legal compliance.

Nowadays, capital markets require two critical confidence-building measures, transparency⁹ and board independence¹⁰, for financial participation of the investor. The demand for transparency has led to the development of laws and regulations requiring disclosure through filing with various agencies and timely announcements through recognised channels. Board independence has called for increasing numbers of non-executive directors on a board to monitor checks and

⁵ Companies Act 1855, s 1.

⁶ (1887) 18 Q.E.D. 815

⁷ Ranald Michie *The London Stock Exchange: A history* (OUP Oxford 1998) 70-142.

⁸ *Panorama Developments (Guildford) Ltd v Fidelis Furnishing Fabrics Ltd* [1971] 2 QB 711 (CA).

⁹ L. Lowenstein 'Financial Transparency and Corporate Governance: You Manage What You Measure' (1996) 96 Colum. L. Rev. 1335, 1361-1362; R. La Porta, F. Lopez-de-Silanes, A. Shleifer and Robert Vishny, "Legal Determinants of External Finance" (1997) 52 J. Fin. 1131; R. La Porta, F. Lopez-de-Silanes, A. Shleifer and R. Vishny, "Investor Protection and Corporate Valuation" (2002) 62 J. Fin. 1147.

¹⁰ MJ Jensen & WH Meckling 'Theory of the firm: Managerial behavior, agency costs, and ownership structure' (1976) 3 Journal of Financial Economics, 305-360; D Higgs Review of the role and effectiveness of non- executive directors (2003) London: DTI; KG Corley 'Examining the non-executive director's role from a non-agency theory perspective: Implications arising from the Higgs Report' (2005) 16 British Journal of Management, 1-4; EU Commission On the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board. Commission recommendation, 2005/162/EC; J Gordon 'The Rise of Independent Directors in the United States, 1950-2005: Of Shareholder Value and Stock Market Prices' (2007) 59 Stanford Law Review, 1465-1568.

balances in corporate administration. The traditional role of the company secretary to act as the company's chief administrative officer for filing documents with the Registrar of Companies House continues today. The increasing requirement to disclose corporate information through document filings and timely announcements has made this administrative office indispensable for a company's operations in a rule-based market economy. The role of the company secretary in the UK has gained greater importance than was originally intended, especially in listed companies which need to comply with law and policy to mitigate exposure to legal and reputational risk.¹¹ *This increased responsibility was not a result of the direct duties imposed on the office by the law, or by providing it with more direct legal powers to exercise against other officers of the company.* The driving force for the increased importance of the company secretary has been the developments in the law requiring greater transparency and more precise governance through internal checks and balances. These include splitting the roles of chairman and CEO, and the demand for greater corporate social responsibility that is now required by law, and policy compliance throughout the corporate groups.¹²

The UK Corporate Governance Code, a soft-law operating on the basis of 'comply or explain',¹³ epitomises a de-legalised approach that enhances the role of the company secretary in the facilitation of board independence.¹⁴ Since independent directors play a constantly increasing role in corporate governance,¹⁵ through their close involvement with the board by attending board and other committee meetings, the company secretary is able to act as an interface between the board and shareholder meetings – between, for example, the senior independent director and the minority shareholders. In an increasingly devolved governance system where independent committees carry out functions with a primary aim of removing directors' conflicts of interest, the company secretary can deliver confidence to investors by acting as an interface between the committee and the chairman (an independent role). Risks identified in committee meetings can be fed through the company secretary to the chairman.¹⁶

¹¹ As stated in *Re Maidstone Buildings Provisions Ltd* [1971]1 W.L.R. 1085, at 1092 that 'so far as the position of a secretary as such is concerned, it is established beyond all question that a secretary, while performing the duties appropriate to the office of secretary, is not concerned in the management of the company. Equally I think he is not concerned in carrying on the business of the company'

¹² S Idowu 'Corporate social responsibility from the perspective of corporate secretaries' in S Idowu and W Filho (eds) *Professionals' perspectives of CSR* (Springer Verlage Berlin Heiderlberg 2009) 49-70.

¹³ UK Corporate Governance Code 2014 (CG Code), 4.

¹⁴ K Keasey, H Short, & M Wright 'The development of corporate governance codes in the UK' In K. Keasey, S. Thompson, & M. Wright (Eds.), *Corporate governance: Accountability, enterprise and international comparisons* (2005 John Wiley & Sons: Chichester) 21-42.

¹⁵ Derek Higgs, 'Review of the role and effectiveness of non-executive directors' January 2003.

¹⁶ The secretary tends to serve a longer term than the board directors; and can thus offer a historical view, in the tradition of the company, to both the board and investors.

Services provided by company secretaries can enhance the effectiveness of independent directors in the governance system.¹⁷ Assisting the non-executive chairman in the selection and appointment of non-executive directors and providing an induction and training programme to new directors¹⁸ and advice to non-executive directors, and assisting the non-executive chairman conducting board evaluation can bring confidence to the investors. These responsibilities increase investor confidence, which reduces the cost of raising capital.¹⁹ The reduction of capital results in value-creation to companies.²⁰ These examples show how the non-statutory Code can act as a catalyst for providing valuable corporate secretarial services to companies that benefit both investors and stakeholders.²¹

In 2006, the Companies Act removed the requirement to appoint a company secretary in private companies. The Act requires public companies to have a company secretary, but allows private companies to decide whether or not the position is required according to their own constitution.²² This change in the requirement for private companies was due to the streamlining of private companies' administrative burdens included in the law, resulting in fewer filing and reporting requirements for private companies.²³ The Corporate Governance Code does not apply to private companies because board independence is less of an issue for them. Policy compliance to mitigate exposure to reputational damage primarily concerns listed companies. Private companies do not operate in other jurisdictions through subsidiary operations so have less concern for

¹⁷ Principle A.5.3 of the CG Code states that a company secretary should be 'responsible to the board for ensuring that board procedures are complied with.'

¹⁸ ICSA Guidance on induction of directors, Guidance Notes June 2012.

<https://www.icsa.org.uk/assets/files/pdfs/guidance/Guidance%20notes%202012/Induction%20of%20directors.pdf>

¹⁹ Romilda Mazzotta & Stefania Veltri 'The relationship between corporate governance and the cost of equity capital. Evidence from the Italian stock exchange', (2014) 18 *Journal of Management Governance* 419–448; K Chen, Z. Chen, and K Wei 'Legal protection of investors, corporate governance, and the cost of equity capital' (2009) 15 *Journal of Corporate Finance* 273–89.

²⁰ Regarding one of the causes of the 2007-09 financial meltdown, it has been stated that "Sometimes what the directors of financial institutions were being asked to consider was just so complicated that a lot of the non-execs didn't understand what was being suggested, and then it became difficult for them to question anything." In such situations, the company secretary can act as a filter to review the relevant documents and determine whether the right types of information have been provided to the directors who, by definition, are not involved with the company on a daily basis.

²¹ Principle A.5 of the CG Code addresses 'information and professional development', and the supporting principles state, 'Under the direction of the chairman, the company secretary's responsibilities include ensuring good information flows within the board and its committees and between senior management and non-executive directors, as well as facilitating induction and assisting with professional development as required. The company secretary should be responsible for advising the board through the chairman on all governance matters.'

²² In Singapore, a company secretary is required for both public and private companies.

²³ David Milman 'The regulation of private companies in UK law: current policy developments and recent judicial rulings' (2009) 257 *Company Law Newsletter* 1-4.

subsidiary governance. For these reasons, whether a company secretary would bring value to private companies can be decided by their members.²⁴

Part II Company secretary as an independent gatekeeper

The company secretary, as a corporate governance officer who aims at fulfilling the corporate transparency requirement and facilitating board independence, should retain the critical attribute of independence as do other gatekeepers such as the auditor, the lawyer, and the compliance officer. However, this attribute of independence should be regulated in order to best realise governance goals.

Compliance officer

As mentioned, transparency is an indispensable element of modern corporate governance, and transparency has been translated into various requirements for filing, reporting of law and policy compliance, and timely announcement. Company directors and company secretaries, as officers of the company, assume filing duties under various laws. These filing, reporting and announcing requirements require independent judgment to be exercised. For instance, complying with accounting rules,²⁵ complying with rules specifically designed to protect the shareholders ie the pre-emptive rights regime,²⁶ understanding the operations of nominee companies to identify rightful investors,²⁷ the application of proxy rules to increase shareholder engagement²⁸ and proactive development of governance protocol to hedge risks stemming from subsidiary operations,²⁹ all demand a skilled governance officer. In future, companies may be required to make disclosures under the freedom of information law if they carry out works that are categorised as public services.³⁰ Independent judgment would be needed to determine issues concerning disclosure requirements.

²⁴ Private companies can determine in their own constitutions whether to utilise such an office in delivering its organisational objectives. According to Companies House statistics, the number of companies incorporated without a company secretary since 6 April 2008 has increased greatly.

²⁵ Company secretaries must ensure that companies' account records are prepared in the form required by company law and accounting standards. Corporate governance structures also affect the accounting decisions. See Tamer Elshandidy & Ahmed Hassanein 'Do IFRS and board of directors' independence affect accounting conservatism?' (2014)24(16) *Applied Financial Economics*, 1091-1102.

²⁶ Chapter 3 of CA 2006 on shareholders' rights on preemption.

²⁷ For the policy discussion on indirect investors' enforcement of corporate governance see RC Nolan 'Indirect Investors: A Greater Say in the Company?' (2003) 3(1) *Journal of Corporate Law Studies*, 73-121.

²⁸ Tsjalle van der Burg and Aloys Prinz 'Empowering small shareholders: a comparison of three instruments' (2006)14(5) *Corporate Governance* 406-417; Paolo Santella, Enrico Baffi, Carlo Drago, & Dino Lattuca 'Legal obstacles to institutional investor activism in the EU and in the US' (2012) vol 23(2) *European Business Law Review* 257-307.

²⁹ Geoffrey C. Kiel, Kevin Hendry and Gavin J. Nicholson 'Corporate governance options for the local subsidiaries of multinational enterprises' (2006) vol 14(6) *Corporate Governance* 568-579.

³⁰ Simone Mezzacapo 'The right of access to public bodies' records in Italy and UK "Actio Ad Exhibendum" and freedom of information risks and opportunities for private sector companies' (2006)17 (4) *European Business Law Review* 959-979.

Furthermore, there are other regulations aiming at removing directors' conflicts of interest and preventing directors' self-dealing. The duty of enforcing these regulations internally falls on the company secretary who shields the company from insider misconduct. Under the Financial Services and Markets Act 2000,³¹ the company secretary also has a role in implementing and communicating procedures for listed company directors to comply with the Model Code on share dealing. To prevent insider dealing by directors,³² prior reporting and obtaining clearance from a non-executive director should pass through the company secretary so that a record can be kept of any communication.

In some companies, company secretaries act also as a gatekeeper to prevent illegal political donations.³³ The UK Companies Act prohibits political donations by UK registered companies and subsidiaries of the ultimate UK holding companies, unless they are authorised by shareholder resolutions in a general meeting.³⁴ The company secretary needs to be familiar with the operations of subsidiary companies both at home and abroad³⁵ in order to design an effective reporting line so that shareholder resolutions can be obtained in a timely manner³⁶ and meet disclosure requirements.³⁷ Through internal corporate governance protocol or a subsidiary's company constitution, group companies can be required to return a certificate to the holding company secretary each year stating either that no payment has been made or providing details when a payment has taken place. The company secretary is the 'go to' person and oversees reporting duties for subsidiaries. These results are then reported annually to the audit committee of the company as well as in an interim report to the committee of independent directors.³⁸

Chief of staff to the chairman

For listed companies, investor confidence is increased by the company secretary's role of enhancing the monitoring and advisory functions of non-executive directors, in a similar way to the greater independence of directors.³⁹ To whom a company secretary reports makes a difference to the governance

³¹ S 96B, The Financial Services and Markets Act 2000.

³² S Djankov, R. La Porta, F. Lopez-de-Silanes, and A. Shleifer 'The law and economics of self-dealing' (2008) *Journal of Financial Economics* 430-65.

³³ Jack Davies 'From gentlemanly expectations to regulatory principles: a history of insider dealing in the UK: Part 1' (2015) 36(5) *Company Law* 132-143.

³⁴ Richard Williams 'Regulating political donations by companies: challenges and misconceptions' (2012) 75(6) *Modern Law Review* 951-980.

³⁵ Companies Act 2006 Part 14. A holding company is permitted to seek authorisation of donations and expenditure in respect of both the holding company itself and one or more subsidiaries through a single approved resolution.

³⁶ Companies Act 2006 Part 14 s 366.

³⁷ Under the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008, Directors' reports must disclose any relevant political donations or expenditures. SI 2008/410 7 Schs 3,4, and 5.

³⁸ This is the current practice of the British American Tobacco. It requires that any donation must be authorised by the board of the company. Such a donation must be fully documented in the company's books.

³⁹ Rafel Crespí-Cladera and Bartolomé Pascual-Fuster 'Does the independence of independent directors matter?' (2014) 28(1) *Journal of Corporate Finance* 116-134.

system. In the UK, the office of the company secretary is often established under the non-executive Chairman's office - acting as chief of staff to chairman.⁴⁰ This coincides with several oversight functions with the Chairman- including the responsibility of conducting the board evaluation.⁴¹ The attribute of independence, by not working under the control of the executive office, enhances the functions of the non-executive directors whose major role is to remove conflicts of interest of the executive directors. Since neither the auditor nor the internal or external lawyers attend board meetings and have no direct access to the chairman and other non-executive directors, the company secretary as compliance officer has a unique gatekeeping role. This role has been recognised as long ago as 1993 in the Cadbury Report, which recommended that the company secretary should give guidance to the board on board members' responsibilities. Board members should have access to the company secretary for such guidance and advice. In particular, the chairman, who is responsible for the functioning of the board, should have strong support from the company secretary. The company secretary's attribute of independence would not have been as necessary if board meetings were simply a management discussion forum without the aim of checks and balances for investors. For instance, the senior non-executive directors should be the channel for a minority shareholder who wishes to communicate with the board. Combining the roles of law and policy compliance, the company secretary is in a position to detect insider misconduct through an effective reporting system and can 'whistle-blow' insider misconduct to the chairman.⁴²

One of the appraisal criteria for the performance of a company secretary is the effectiveness of internal controls. If the internal control system has failed, the board can reprimand the company secretary publicly and thus deter reckless conduct by members of the executive team.

Enforcement of independence

As a gatekeeper and a business advisor, a company secretary must exercise independent judgment to provide value to the company. For instance, their responsibility for filing and reporting to regulators and the revenue office carries over into a duty to promote the success of the company as an officer and an employee who ensures compliance with statutory duties. A company secretary would be held liable if he or she failed to take steps to prevent the contravention of statutory provisions, such as the board failing to make trading disclosures.⁴³ When company secretaries assist the non-executive directors to enhance their monitoring and advisory roles, they must act independently of the executive

⁴⁰ Caroline Newsholme 'FRC guidance on board effectiveness' (2011) 35(2) *Company Secretary's Review* 14-15.

⁴¹ OECD, Corporate Governance Principle VI E4; UK Corporate Governance Code Section B.6.

⁴² Indira Carr, David Lewis 'Combating corruption through employment law and whistleblower protection' (2010) 39(1) *Industrial Law Journal* 52-52; Peter Yeoh 'Whistleblowing: motivations, corporate self-regulation, and the law' (2014) 56(6) *International Journal of Law & Management* 459-474.

⁴³ CA 06 s 84(1).

directors in advising the non-executive chairman and the independent committees.⁴⁴

As a general duty, UK law requires directors to act independently by exercising unfettered judgment.⁴⁵ Similarly, a UK auditor certifying a company's accounts and directors' reports should also act independently.⁴⁶ No such duty is imposed in law on the company secretary. Whether such a duty should be legally imposed on the company secretary depends on their functions vis-à-vis the board, the organizational objectives, and corporate governance agenda. The company secretary may act as chief of staff to the non-executive chairman, an advisor to the board, a critical appraiser of board members' roles, a third person in a chairman-CEO relationship, an interface between the board and the shareholders, a gatekeeper for corporate governance. *If these roles are to remain open for organizational innovation, the duty of independence does not need to be legally prescribed.* This way would allow companies to design the job descriptions freely without being caught out unnecessarily by the strict legal rules.⁴⁷ Hence, a code of conduct with a situational approach to the meaning of 'independence' – using the negative criteria as the Corporate Governance does for independent directors – can be issued.⁴⁸ In addition, there can also be systems and processes to ensure the quality of independence, notably, on the appointment to, and removal from office.⁴⁹

If the company secretary is expected to be a corporate gatekeeper in a similar way as an auditor, the appointment and removal of an auditor could offer an equivalent way of proceeding. Thus, since an individual director cannot unilaterally dismiss an appointed auditor, an individual director should also not be able to remove the company secretary, leaving only the board with the ability to appoint or remove the company secretary. As the law places greater control on the appointment and removal of a company's auditor for greater investor confidence, auditor rotation, the control of auditors' remuneration, control procedures for limiting auditors' liabilities to the company, and shareholder participation in appointment and removal processes all help to ensure auditor independence. Although there is no hard law in the UK giving the effect of regulating a company secretary's independence, the UK Corporate Governance Code recommends that only the board should have the ability to appoint and remove a company secretary; an individual director should not be able to do so unilaterally.⁵⁰

⁴⁴ UK Corporate Governance Code B.5.2.

⁴⁵ CA 06 s 173.

⁴⁶ APB Ethical Standard 1 (revised) on integrity, objectivity, and independence (2008), <http://www.frc.org.uk/images/uploaded/documents/ES1%20-%20v5%20clean.pdf>.

⁴⁷ Principles-based regulation can be considered. See Julia Black, Martyn Hopper & Christa Band 'Making a success of Principles-based regulation' (2007) 1(3) Law and Financial Markets Review 191-206.

⁴⁸ The Code of Corporate Governance uses the same situational approach to define when a non-executive director is not independent.

⁴⁹ Some lessons can be learnt from auditor's appointment and removal to maintain audit independence. See Reiner Quick 'EC Green Paper proposals and audit quality' (2012) 9(1) Accounting in Europe 17-38.

⁵⁰ UK Corporate Governance Code B.5.2.

A company secretary can be a permanent employee of a company, unlike an auditor (a contractor) or a company director of a listed company, whose term of office is usually based on a service contract of some limited period. Subjecting company secretaries to similar controls could disrupt the administrative operation of companies, including the strict filing and reporting duties required by the law. If the removal and appointment of a company secretary requires shareholder approval at a general meeting,⁵¹ the board will be unable to quickly suspend a company secretary who is found to be in default of compliance with the law or of his or her contractual or other duties to the company. In an interim period, such a company may need to fulfil its filing duties urgently, and convening a meeting to obtain approval of the company's shareholders can cause missed filing deadlines, with a consequent contravention of the law for which directors would be liable.⁵²

In this way, although the governance of an auditor's independence offers some lessons for regulating the independence of the company secretary, the auditor's model may not be entirely appropriate for the company secretary. Auditors have the right to make representations to the shareholders who vote on the question of their removal.⁵³ A similar arrangement could be set up for the removal of a company secretary. Prior to the authorisation of their removal, they can make a written or oral representation to the board. Since their removal is not by ordinary resolution, a representation to the general meeting may not be justified. A representation can be included in the company's annual report.

This soft law approach to regulating the role of company secretary with the emphasis on disclosing company policy as well as setting up formal procedures for appointment and removal would allow independence to be enhanced within the board and the company.

Part III The prospects and legal challenges of provisional services firms

Professional services firms

It is debatable whether a permanent employee or a contracting professional firm would better fulfil the role of gatekeeper. An employee company secretary is closer and more integrated with the board and the company than an auditor. The company secretary has closer proximity to the shareholders, hence is in a better position to act as spokesperson for the board in communicating with shareholders. An employee company secretary holds a longer tenure than executive directors and, having experienced both good and bad times, is also a better repository of corporate memory which is invaluable for providing guidance to a board.⁵⁴

⁵¹ This is currently required for a removal of the auditor.

⁵² CA 2006 s 541.

⁵³ CA 2006 s 511(3)

⁵⁴ The Company Secretary: Building trust through governance, 2014 ICSA <https://www.icsa.org.uk/products-and-services/knowledge-and-guidance/research/the-company-secretary-report>

On the other hand, because many corporate gatekeeping functions are now being taken up by outside contractors, professional firms can provide company secretarial services. In fact, private companies, and also some listed companies, have long been using professional services firms to fulfil their statutory requirements. This includes the appointment of professional services firms to act as company secretary, outsourcing some part of the work to the firms, or retaining them as back-up support.⁵⁵ As UK law does not require a company secretary be a full-time employee or an individual person, a body corporate providing secretarial services can be appointed as the company secretary. The benefit of having a corporate company secretary is that it provides flexibility by enabling more than one person to represent the company and also gives access to a more extensive knowledge base. Similarly, a professional firm in the form of a partnership or limited liability partnership (LLP) can also provide such services. Professional services firms can have greater expertise and knowledge in particular areas of governance rules, such as the listing and compliance requirements for stock exchanges. A company does not need to employ a full-time person to hold the office and can contract the service out to a professional firm to be more cost-effective. If a company needs specialised knowledge - in financial law, for example - a law firm can provide the service. A lawyer can be retained by a company to hold the office of company secretary. A company faced with budgetary constraints may not wish to employ a full-time company secretary. Such retainers are generally welcomed by law firms because they allow the law firms to become familiar with the company and to forge a good business relationship with it.⁵⁶ In such cases, the company is free to design its own job description, and the professional services firm can provide tailor-made secretarial services. Market competition between firms allows companies to obtain cost-effective secretarial services.⁵⁷

Two major issues arise. As with audit firms, market competition, a driver thought to deliver innovation, can compromise the element of independence that is critical for the gatekeeping service.⁵⁸ The company secretary's independence is fundamental to corporate value creation. However, how can secretarial quality be maintained and enhanced in this respect if the provision of the service is subject to market competition? And also, how should a company secretary's act and liability be attributed to the entity chosen by the professional services providers ie a company, an LLP, or a partnership? Is it to the company or the firm that provides the service, whether ordinary or limited liability partnership? Professional services firms, which potentially hold assets,⁵⁹ are more likely to become a source of compensation than an individual employee with limited

⁵⁵ This is the case especially at times of peak company secretarial activity e.g. year-end/AGM.

⁵⁶ Such a secondment arrangement can provide mutual benefits. See Secondment plan of mutual benefit (1992) 6(47) Lawyer 6.

⁵⁷ Christopher Humphrey 'Regulating audit beyond the crisis: A critical discussion of the EU Green Paper' (2011) 20(3) The European Accounting Review 431-457.

⁵⁸ K Houghton and C Jubb 'The Market for financial report audits: Regulation of and competition for auditor independence' (2003) 25(3) Law and Policy 299-321.

⁵⁹ Companies can provide indemnities to corporate officers i.e. company directors. The auditor can also enter into a damage limitation agreement with the audited company to control their financial if not reputational exposure.

assets. Since April 2005, companies can now freely provide indemnities to a secretary as they see fit. If this can apply to professional services firms, some controls should be established to ensure that service quality is not unduly compromised.

Maintaining the attribute of independence

Many professional services firms provide a large range of corporate services to companies including audit, management, tax, secretarial and legal services. The issue of auditor independence has been raised when an auditor, acting as an external gatekeeper, plays 'low ball' to gain other non-audit businesses.⁶⁰ Such market competition is essential to service innovation, but it can also compromise some of the key requirements for maintaining good corporate governance and creating corporate value. When an independent audit is compromised, market competition fails to deliver value, not only as an engine for innovation but also as an alternative regulatory tool for quality control. There are many ways to regulate conflicts of interest when a professional services firm is engaged to provide secretarial services. Company secretarial and other management consulting services are more likely to be among the additional businesses that can be gained from audit 'low-balling' practices. The issue is how to make sure that the secretarial services offered are not 'tagged along' with the audit service. Potential conflicts can be controlled by the company disclosing such a 'tag-along' relationship. Once the tag-along relationship has been disclosed, shareholder approval can be required to further examine potential conflicts and the value provided to the company. Furthermore, such approval may only need to be required for services provided by the professional services firms who offer a full range of services. Compulsory rotation can be introduced to maintain a more arms-length relationship between the company and professional services firms. Rotation can also increase independence since the company secretary will be less attached to the management team, hence fostering a more arms-length relationship. Furthermore, UK whistleblower protection law also applies to contractors.⁶¹ This law further strengthens professional services firms' ability to maintain the quality of independence.

There is a further issue regarding a service firm's liability for conflicts of interest. If, as discussed in the previous section, company secretaries are contracted to provide value-added services such as appointment of non-executive directors, designing a cost-effective reporting system or a compliance monitoring programme, a professional services firm providing the same secretarial services to competing companies at the same time may give rise to a claim for a conflict of interest. This is because the firms will have access to sensitive commercial information when they attend board meetings and can access information about subsidiaries through the governance protocol or by virtue of the subsidiary's

⁶⁰ Patrick Velte and Carl-Christian Freidank, 'The link between in- and external rotation of the auditor and the quality of financial accounting and external audit' (2015)40(3) European Journal of Law and Economics 225-246.

⁶¹ In the US, whistleblower protection is not given to at-will employees.

constitution.⁶² For a partnership firm, an internal wall created to absolve potential conflicts may be needed. Such a 'Chinese wall' may be more effective for managing the risk of conflicts between, say, the audit and secretarial departments. Whether such a wall can also be effective when raised within the secretarial department is questionable. Would disclosure of the conflicts by the firm and client consent be sufficient to remove the liability? Disclosure by the firm and client consent may remove the conflicts if the secretarial service is purely administrative, but if the work includes more business-oriented services, for instance involvement in the recruitment of non-executive directors, such conflicts are not easily removed. When a law firm being retained to act as company secretary is tasked with monitoring a corporate compliance programme, this may create a conflict if the firm is also retained by a competing company.

The UK Companies Act 2006 deals with this problem to some extent. Under S 1214 (2) of the Act, the auditor of a company cannot also be the company secretary. But this does not completely solve the potential for conflicts of interest. If a company appoints an auditor from a particular services firm, this would not prevent another person from the same services firm from acting as company secretary.

Attribution and professional firms' liabilities

Clarifying firms' potential liabilities is crucial. For criminal liability, the Companies Act 2006 imposes criminal liabilities on the company secretary,⁶³ therefore not having a clear approach to identifying the person to be held accountable would defeat the deterrent effect of the criminal sanctions. For civil liability, identifying the right accountable person affects the remedies to be awarded to injured parties.

Criminal liability

Secretarial services can be provided by a professional firm, which can be a body corporate (including a limited liability partnership⁶⁴) or a partnership. The law states that it is possible for an officer of the company to be held civilly and criminally liable. If the professional services firm has a legal personality, such as a company or an LLP, the question is how to attribute liability to the person appointed as the company secretary. Also, when a company engages a partnership firm i.e., an LLP (a separate legal entity from its members) to provide services, who is the person, in fact and in law, appointed to hold the office of company secretary?

⁶² Ben Walther 'Bylaw governance' (2014) 20 Fordham Journal of Corporate & Financial Law 399- 459.

⁶³ For instance, CA 2006, s 26(3), s 32(3), s 425, s 451, and Part 36 (Offences under the Companies Acts).

⁶⁴ Limited Liability Partnerships Act 2000 s1(2).

In the UK, a body corporate can be made criminally liable.⁶⁵ Under the Companies Act 06, when a person is an officer of another company, he or she does not commit an offence as an officer in default unless one of the company's officers is in default. The provision can be taken to mean that the company providing the secretarial services, by holding the office of company secretary, cannot be held criminally liable under the Act unless a director of the professional services firm is identified as an officer in default by authorising, permitting, participating in, or failing to take all reasonable steps to prevent the contravention. Nevertheless, a director of a professional services firm may not be personally involved in the provision of the service, and in that case the director's firm will not be held criminally liable. The current provisions of the Act can make the application of the attribution rules confusing.

When the services firm is a partnership or limited liability partnership, an individual member of that firm will serve as the company secretary and thus, criminal liability is assumed by the individual rather than the firm. However, because a limited liability partnership acquires a separate legal identity, if the company engages the services firm rather than an individual from the services firm, a similar question can arise. Neither the Act and nor case law have yet considered such a situation. A clear legal framework on attributing individual behaviour or liability to the entity (or association) of the professional services firms should be introduced.

Civil liability

In terms of civil liability, the company or its shareholders⁶⁶ through a derivative claim can pursue compensation claims or a claim to account for profits against the firm and/or the individual from the firm providing the service. If the professional services firm is a body corporate such as a company, claims can be made against the company. If the firm is an entity other than a company, claims in contract or in tort brought to obtain compensation will depend on the organisational form of the firm – whether the individual is liable or all the members of the partnership could be claimed against. If an LLP is retained to act as the company secretary, the contract is between the company and the LLP, which is a body corporate under UK law. An action for damages should be brought against the LLP. There can be an indemnity provision in the contract. Yet, an action in tort can be brought against the individual person providing the service.

Part IV Transnational governance and combination with the office of general counsel

Transnational governance and the resulting synergies

There are a number of jurisdictions that require the office of company

⁶⁵ Criminal Justice Act 1993 s 52 and Enterprise Act 2002 s 188.

⁶⁶ CA 2006 Part II.

secretary.⁶⁷ As multinational companies are becoming the main providers of goods and services, the company secretaries' tasks are to design effective subsidiary governance framework to mitigate harms and to create governance synergies. These synergies are delivered in the situation of actual or potential joint law enforcement actions against the multinational companies. In actual joint law enforcement, company secretaries are the first contact point for responding to regulatory and enforcement enquiries across many jurisdictions. In potential joint law enforcement actions, their role is to ensure that measures, as such a subsidiary governance framework,⁶⁸ are in place to prevent enforcement actions or to defer an enforcement action in the case of a deferred enforcement action agreement.⁶⁹

Within a multinational company, if general counsel also serves as company secretary the legal office can be organised to include the company secretaries of subsidiaries incorporated in different jurisdictions. Many UK companies have combined the offices of company secretary and corporate counsel.⁷⁰ Of the FTSE 100 companies surveyed in a census,⁷¹ 70.2% of the company secretaries held a legal qualification. Under a subsidiary governance framework, the subsidiary company secretaries can provide needed information (e.g. a certificate of political donations) to the general counsel of the parent company and can assist the general counsel with implementing procedures as required by law (e.g. an anti-bribery programme) for the subsidiary companies. A governance structure designed to allow the company secretary of the parent company to supervise, through a reporting line, subsidiary companies' secretaries can effectively ensure improved information-sharing across the group organisation. In increasing joint enforcement by multi-jurisdictional enforcement agencies, a global settlement agreement with a reform programme would be cost-saving strategy for a defaulting company. This combination of the two offices would make it easier for monitored parent companies to conduct due diligence on other group affiliates.⁷² A general counsel or a legal officer is not required in the UK and in many other jurisdictions, yet many large companies and multinational companies have general counsel offices or legal departments that manage the company's legal affairs. If a general counsel or legal officer is not a legally installed officer within the organisation, this person may not have access to, or the power to obtain corporate information. Legally, the general counsel does not have access to the boardroom, but such access can be gained through becoming the company secretary. Thus, the general counsel may request information from

⁶⁷ Ireland, Australia, New Zealand, Hong Kong, Singapore, China and USA (ie State of Delaware under s 142(a) of the Delaware General Corporation Law).

⁶⁸ Federico Mazzacava 'Justifications and Purposes of Negotiated Justice for Corporate Offenders: Deferred and Non-Prosecution Agreements in the UK and US Systems of Criminal Justice' (2014) 78 (3) *Journal of Criminal Law* 249-262.

⁶⁹ The company secretary can also be the designated person to monitor a deferred statement programme.

⁷⁰ Ian Maurice of Egon Zehnder discusses the relationship between General Counsel and Company Secretary and describes the UK trend to split these roles http://www.egonzehnder.com/files/the_general_counsel_and_the_board.pdf

⁷¹ The census was carried out in 2004 by Equiniti.

⁷² Deborah DeMott 'The Crucial But (potentially) precarious position of the chief compliance officer' (2013) 8 *Brookings Journal of Corporate Finance and Compliance Law* 57-70.

a subsidiary company's in-house counsel who does not have the legal power to access the company's information. However, a company secretary who is an officer of the company would have such power, and obtaining corporate information such as records or sales data would not need to be authorised by the executive directors - to whom general counsel is affiliated.

UK companies are required to implement internal procedures under various acts to protect the stakeholders of the company and safeguard the interests of the general public. Companies are required to put in place health and safety procedures to protect employees and to implement an anti-corruption system within the organisation, including subsidiary companies incorporated in other jurisdictions. Company secretaries involved in the design and the implementation of these procedures who work collaboratively with other company secretaries of the same group under, say, the general counsel's office, would ensure that the norms of the parent company are effectively diffused through the subsidiary companies. These norms can also result in a spillover effect on the business environment surrounding the subsidiary companies. These procedural mechanisms not only create a safe harbour if there is misconduct by an employee or an agent of the company and its subsidiaries. They may be required by regulators as a condition for a deferred prosecution.⁷³

The problem of wearing two hats

When a person serves as both general counsel and company secretary of a single company, it is difficult to make a precise distinction between the functions and roles of the two posts. The law requires a company to appoint a secretary, but it does not require general counsel. Yet a general counsel acts as an independent legal adviser to a company, and legal advice given to the company receives privileged protection against disclosure.⁷⁴ A company secretary, however, is an officer of the company rather than an independent legal adviser and any advice given, even if legal, is not protected by the legal privilege rules. Legal privilege rules confer protection on companies against the disclosure of internal communications otherwise required by third parties. A company secretary may have a duty to report to the regulator and may make a public interest disclosure of misconduct by the company, or an insider of the company, to the regulator while receiving protection. Yet, general counsel does not have such a duty and may not make a public interest disclosure while receiving protection. Therefore, it is understandable for a general counsel to hold the office of company secretary, even if not all of the advice given to the board or individual officers of the company in internal communications can be classified as legal advice. There is an advantage for companies to appoint a legally qualified person to act as the company secretary.

⁷³ Jessica Naima Dijlani 'The British importation of American corporate compliance' (2011) 76 *Brookings Law Review* 303- 341.

⁷⁴ *Three Rivers District Council -v- Bank of England* (No. 5) [2003] QB 1556 and *Three Rivers District Council -v- The Bank of England* (No. 6) [2005] 1 AC 610.

Communication privilege against disclosure given to the company secretary

The Corporate Governance Code specifies that the company secretary should be accessible to board members for advice.⁷⁵ If so, would advice given to individual non-executive directors on their rights and duties constitute legal advice? Such protection may encourage non-executive directors to seek the advice of general counsel or outside counsel on an issue. Based on such advice, non-executive directors can make legally informed decisions. Without such legal privilege protection, members of the board would not only be less willing to use the company secretary for internal governance advice but also less willing to share information with them.

Should privilege protection cover internal communications between a non-lawyer company secretary and the company, or the individual directors, to enhance corporate value? In all the work carried out by the company secretary of a listed companies, they must put on legal spectacles when providing their services; be it formulating governance protocols and instituting reporting systems to improve governance standards or evaluating governance strategies and best practice. They also act as a liaison between the board and management. Without such protection, officers may be discouraged from seeking advice from a non-lawyer company secretary. If a non-lawyer company secretary is not used by other officers for internal advice this would reduce the company secretary's ability to give advice on governance issues. In particular, if the company secretary acts as chief of staff to the chairman and also as the executive and non-executive directors' link to the chairman, protection given to their communications would enhance greater information-sharing at that level. Such protection (e.g. providing confidentiality for internal communications) would level the playing-field for non-legally qualified company secretary who can provide an enhanced level of governance compared with a general counsel who is normally attached to the CEO's office.

Conclusion

The transformation of the UK company secretary from a mere servant to a corporate gatekeeper has been spurred on by the development of capital markets that have been demanding higher levels of corporate transparency and board independence. Soft-law based corporate governance has enhanced the gatekeeping functions of the company secretary in facilitating corporate transparency through law and policy compliance and board independence through assisting oversight by non-executive directors. Their attribute of independence can benefit from a soft-law approach to regulation. A professional code of conduct can be developed to provide situational guidance on the attribute of independence. The Corporate Governance Code can include a regime on the appointment and removal of a company secretary – including the right of representation to the board of a removed company secretary, and on conflicts of

⁷⁵ Corporate Governance Code, B 5.2.

interest that may arise when appointing a professional services firm as company secretary. More definite rules on corporate attribution in civil and criminal liabilities should be introduced to increase the utility of professional services firms in the provisions of such a gatekeeping service. Some amendment to the current provisions in the Companies Act 2006 should be made to avoid a confusing reading. While combining the offices of general counsel and company secretary can yield governance synergies, e.g. through a subsidiary governance framework, a non-legally qualified secretary can also bring a different set of skills to companies in assisting the governance programme. Giving protection to communications between the company secretary and board members can increase the ability of the company secretary to give guidance in matters of governance.