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Company Dissolutions - Capital v Income Distributions and the Impact of ESC C16

When a company reaches the end of its useful life, it is generally wound up, although it is quite possible to just leave a company and it remains dormant.

s.652

If the decision is to have the company struck off the register held at Companies House, it is possible to avoid being involved in a formal winding up procedure under the Insolvency Act 1986 (as amended), by either:

- asking the Registrar of Companies to strike the company off the Register and so dissolve it under Section 652 Companies Act 1985 (“s.652”), or
- becoming inactive and waiting to be struck off and dissolved.

Dissolution under s.652 should not be referred to as a winding-up nor as an ‘informal liquidation’.

If distributions are made as part of one of the two dissolution processes above, there is no winding up and therefore such distributions will normally be treated for tax purposes as an income distribution within s.209 ICTA 1988.

*“a capital distribution outside formal winding up is **unlawful**”.*

ESC C16

However, by virtue of Extra Statutory Concession (“ESC”) C16, providing certain assurances are given to the Inspector before the event, the Revenue is prepared for tax purposes to regard the distribution as being a return of capital as if made under a formal winding-up and a liability under s.209 ICTA 1988, will not arise on the distributions of assets to shareholders.

In order to qualify the company must satisfy the Inspector that:

- it does not intend to trade or carry on business in the future; and
- it intends to collect its debts, pay off its creditors in full and distribute any balance to its shareholders (or has already done so); and
- it intends to seek or accept striking off and dissolution

In addition, the company and its shareholders must agree that:

- they will supply such information as is necessary to determine, and will pay, any corporation tax liability on income or capital gains; and
- the shareholders will pay any capital gains tax liability (or corporation tax liability in the case of a corporate shareholder) in respect of any amounts distributed to them in cash or otherwise as if the distribution had been





made during a winding-up.

Notwithstanding the tax treatment of capital distributions in striking off under ESC C16, the making of a capital distribution outside a formal winding up remains **unlawful**.

Bona Vacantia

If there is an unauthorised return of capital to shareholders, the company has the right to recover the money from its members under Section 654 of the Companies Act 1985, which would pass to the Crown as Bona Vacantia when the company is dissolved. Therefore, the Crown, acting through the Treasury Solicitor would be entitled to recover that distribution from the members.

The only legal way to avoid this “right” passing to the Crown as Bona Vacantia is to put the company into formal liquidation prior to dissolution, or legally reduce the amount of the share capital prior to the company dissolution.

In March 2007, the Treasury Solicitor issued the second version of Guidelines setting out circumstances where, as a

concession, the Treasury Solicitor will waive the Crown’s right to any funds distributed to members prior to dissolution if:

- a company has been struck off under Section 652A of the Companies Act 1985; and
- the shareholders have taken advantage of the ESC C16; and
- the amount of the share capital distribution is less than £4,000.

The Guidelines specifically states that if the amount of the share capital exceeds £4,000, the company should be put into liquidation prior to dissolution, or steps taken to legally reduce the amount of the share capital to below £4,000 prior to the dissolution of the company.

The Guideline’s reference to “unauthorised returns” of capital that may become Bona Vacantia, only applies to distributions of share capital (which would include share premium and any non-distributable reserves) and not capital distributions.

Therefore, the £4,000 limit only applies to distributions of share capital and not to capital distributions in general and

thus for most private companies, whose share capital is less than £4,000, capital distributions of any amount can continue to be made under ESC C16/Section 652 procedure without the need to be concerned about Bona Vacantia issues.

If you have any questions arising from this technical guidance note or wish to discuss how to place a company into solvent liquidation please contact either Tony Mitchell or Brett Barton at Cranfield Business Recovery who will be happy to be of assistance.

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