



ICAEW TAX FACULTY REPRESENTATION

TAXREP 18/11

EXTRA STATUTORY CONCESSIONS – FOURTH TECHNICAL CONSULTATION ON DRAFT LEGISLATION

Comments submitted on 7 March 2011 by the Tax Faculty of the Institute of Chartered Accountants in England and Wales on the proposed legislation to replace existing extra statutory concessions published in a consultation document in December 2010

Contents	Paragraph
Introduction	1–3
Who we are	4–6
Extra Statutory Concession C16 Dissolution of companies under s652 and s652A Companies Act 1985	7–29
The Tax Faculty's ten tenets for a better tax system	Appendix 1

EXTRA STATUTORY CONCESSIONS – FOURTH TECHNICAL CONSULTATION ON DRAFT LEGISLATION

INTRODUCTION

1. This document sets out the comments of the Tax Faculty of the Institute of Chartered Accountants in England and Wales (ICAEW) on the proposed enactment of extra statutory concessions as set out in the consultation document published on 13 December 2010.
2. Our comments are restricted to only one of the extra statutory concessions covered in the consultation document, namely C16 Dissolution of companies under s652 and s652A Companies Act 1985.
3. Information about the Tax Faculty and the ICAEW is given below. We have also set out, in Appendix 1, the Tax Faculty's ten tenets for a better tax system, by which we benchmark proposals to change the tax system.

WHO WE ARE

4. The Institute operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 132,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 775,000 members worldwide.
5. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The Institute ensures these skills are constantly developed, recognised and valued.
6. The Tax Faculty is the focus for tax within the Institute. It is responsible for technical tax submissions on behalf of the Institute as a whole and it also provides various tax services including the monthly newsletter *TAXline* to more than 11,000 members of the Institute who pay an additional subscription, and a free weekly newswire.

ESC C16 – Dissolution of companies under s652 and s652A Companies Act 1985

7. Extra statutory concession (ESC) C16 is used on a regular basis by a considerable number of taxpayers.
8. It allows them to wind up a solvent company which is no longer required without the formality and expense of appointing an Insolvency Practitioner to put the company into formal liquidation.
9. We have received a considerable amount of evidence from our members as to the usefulness of this concession. The interest has been confirmed by the number of hits that a posting about the proposed changes has received since it went on our website on 18 January 2011. See <http://www.ion.icaew.com/TaxFaculty/21343> for the posting.
10. In addition we have received a considerable number of emails from ICAEW Tax Faculty members concerned by the withdrawal of what is an extremely useful, and extremely well used, Concession.
11. Our members have cited other benefits from the dissolution option.

Adverse publicity. – If a company is merely struck off, then there is no publicity, and as far as the public (or more importantly personal friends) are concerned the business has ceased typically on the owner's retirement. A liquidation, even a solvent one, has to be publicized, and the public, who don't understand the concept of solvent liquidations are likely to get the wrong idea.

Control – If the company is put into liquidation before all the debtors are collected, the liquidator will be responsible for collecting the debts, which may have a different result, to the owners collecting the debts in. If they wait until all the debts are paid off and then put the company into liquidation this will further delay their payout, see the next point.

Time – If a company decides to cease trading it can apply for an ESC C16 ruling and then as and when the debtors are collected and the creditors are paid they can distribute the surplus cash. A liquidator on the other hand has to advertise and give time for all potential creditors to come forward. The last thing the liquidator wants to do is make a distribution and then find that a creditor or worse a potential claimant emerges. For example a group of former employees might see the liquidator's advert and chose to write in saying they thought they had a potential claim because of some work related illness that might become evident in the future. The liquidator would have to investigate the claims (more cost) and not make a payout until they were satisfied no liability existed, which could take a considerable period of time.

12. The overall concern of our members is that the statutory enactment, as currently proposed, will limit the amount of money that can be distributed to shareholders to £4,000 whereas there is no limit at the present time. The £4,000 agreed limit in BVC 17 was purely in relation to unlawful distributions - it is not relevant for what we presume are the vast majority of ESC C16 cases which will be concerned with amounts that can lawfully be distributed.
13. The effect will be that the statutory provision will be of very little practical benefit to those affected. They will either have to distribute the majority of the funds of the company by way of dividend, on which the shareholders will suffer income tax, or they will be required to put companies into formal liquidation and incur the costs of an Insolvency Practitioner to do so.
14. At a time when the Government is seeking to simplify the tax system, this proposal runs counter to that. We understand from HMRC staff that the Government is concerned that the concession is being 'abused' and that tax is being evaded. This is clearly an issue of major concern if true but would welcome further information on this aspect.

Historical background

15. We understand that the process that became ESC C16 was in existence in the 1970s and was used, as it is used now, to allow companies to be dissolved without the formality and expense of a formal liquidation.
16. Initially if the amount involved in the dissolution was in excess of £1,000 we understand that the local Inspector had to refer the matter to Head Office for the latter's approval.
17. In the mid 1980s there was considerable criticism of the existence of unpublished concessions and draft clauses were introduced in two Finance Bills which would have had the effect of requiring Parliamentary approval for the more important concessions. The government agreed to undertake a review of the (unpublished) concessions then in existence and in May 1985 27 concessions under the control of the Inland Revenue were 'published' amongst them ESC C16.

18. When it was published there was no limitation on the amount that could be distributed using ESC C16. We have no knowledge as to whether the £1,000 limit was continued in an unofficial way.
19. It is clear from what our members have told us that no limit is applied currently and we have been told of several instances where amounts in excess of £500,000 have been 'approved' for distribution to shareholders using the ESC C16 route.

A company law problem

20. A couple of years ago a potential company law problem was identified with ESC C16.
21. For tax purposes a distribution under ESC C16 is treated as liable to capital gains rather than income tax. But if the distribution is not lawful under the Companies Act then the concession is not able to change that unlawful status. So if a company was distributing its share capital, or undistributable reserves, then that is an unlawful distribution and the amount can be reclaimed from the shareholders and returned to the company. If the company has been dissolved before this problem is identified then either the company will have to be brought back into existence, to receive the unlawful distribution, or the unlawful distribution will become *bona vacantia* and can be recovered by the Treasury Solicitor or by Farrer & Co who administer *bona vacantia* for the Duchy of Lancaster and the Duchy of Cornwall.
22. The Treasury Solicitor's Office issued a statement in 2008, BVC 17 Distribution of Company Share Capital, to the effect that if they became aware of the position they would not raise the unlawful distribution issue if ESC C16 had been used and the amount of the unlawful distribution did not exceed £4,000. This was believed to be the average cost of a formal liquidation at that time.
23. It would appear that it is this same £4,000 figure which it is proposed to 'use' in the enactment of ESC C16. It is proposed that this will be the limit of the amount that can be paid out by any company without going through a formal liquidation – this is Condition B as laid down in the proposed enactment.

What is to be done?

24. We are concerned that current ESC C16 is a very simple and straightforward way to 'get rid of' companies that are no longer required and the proposed legislative enactment will create a more burdensome and expensive alternative.
25. It is of concern that tax legitimately payable may be being evaded using ESC C16. We would welcome further information from HMRC as to exactly how the existing concession is being exploited.
26. We believe that HMRC should explore other ways in which the effect of the concession can be retained but with more safeguards to minimise the risk of evasion. This may involve more information being provided at the time the statutory equivalent of the concession is 'granted' so that HMRC can trace, if required, that the tax has been paid by the shareholders. There might even be a withholding on account of the potential tax liability to ensure that the eventual liability will be settled.
27. At the present time the government is seeking ways to remove burdens on business. We do not think that the current solution put forward in this consultation is an appropriate one in the light of that overall government policy approach.
28. However, if the Government is minded to proceed with a monetary 'cap', then we suggest that the £4,000 is increased to a more appropriate amount which will allow small companies to be dissolved without the cost of an Insolvency Practitioner.

29. So if there is to be a financial 'cap' then we recommend that the Condition B in the proposed enactment of ESC C16 should be amended and the current limit of £4,000 increased.

iky March 2011

© The Institute of Chartered Accountants in England and Wales 2011
All rights reserved.

This document may be reproduced without specific permission, in whole or part, free of charge and in any format or medium, subject to the conditions that:

- it is reproduced accurately and not used in a misleading context;
- the source of the extract or document, and the copyright of The Institute of Chartered Accountants in England and Wales, is acknowledged; and
- the title of the document and the reference number are quoted.

Where third-party copyright material has been identified application for permission must be made to the copyright holder.

www.icaew.com

APPENDIX 1

THE TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. **Statutory:** tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. **Certain:** in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. **Simple:** the tax rules should aim to be simple, understandable and clear in their objectives.
4. **Easy to collect and to calculate:** a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. **Properly targeted:** when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. **Constant:** Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. **Subject to proper consultation:** other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. **Regularly reviewed:** the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. **Fair and reasonable:** the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. **Competitive:** tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99.