

**Labour Briefing Notes:
Rating (Coronavirus) and Directors Disqualification (Dissolved Companies) Bill
Prepared by Professor Prem Sikka (15 June 2021)**

OVERVIEW

The Bill¹ is a mixed bag. One part relates to business rates in the post-Covid period and the second relates to insolvency abuses.

It should be noted that the Bill is not a reform of business rates or insolvency practices.

Both elements raise serious questions, which are identified below. The insolvency reforms seem to be headline catching but say little/nothing about some of the implementation problems. Indeed, they can't be fully implemented without a major reform of company formation and Companies House.

THE BILL

1. This Bill has two parts:

- a. Clause 1 concerns the impact of the coronavirus pandemic on business rates. It enables local councils to grant relief to affected businesses.

Business rates are devolved to Scotland, Wales and Northern Ireland. Therefore, Clause 1 has effects in England only.

- b. Clauses 2 and 3 amend existing legislation to make it easier for the Government to investigate misconduct by directors of dissolved companies².

Company law matters are reserved to the UK Parliament in Great Britain so clause 2 extends to England, Wales and Scotland.

Clause 3 makes equivalent amendments for Northern Ireland, for which a legislative consent motion has been sought.

BUSINESS RATES

2. The Rating (Coronavirus) and Directors Disqualification (Dissolved Companies) Bill legislates to ensure that COVID-19 cannot be taken as a cause of material changes of circumstances for business rates.

¹ <https://bills.parliament.uk/publications/41475/documents/202>

² A dissolved company is one that has been struck off the register of companies and has ceased to exist. An application for striking off may be made by the directors of a company under specific circumstances. Alternatively, the registrar of companies may strike the company from the register if they have reasonable grounds to believe that it is no longer trading. A company must be struck off before it is dissolved, and it becomes dissolved three months after the Gazette notice announcing the striking off

The government says that market-wide economic changes to property values, such as from COVID-19, can only be properly considered at general rates revaluations, and will therefore be legislating to rule out COVID-19 related 'material change of circumstance' (MCC) appeals³.

3. Not all businesses affected by COVID-19 are covered by the reliefs previously announced and may struggle to pay business rates amid the ongoing economic uncertainty and some will need support.
4. On 25 March 2021, the government announced that it will give councils £1.5 billion⁴ to offer grant relief to businesses which have been hard hit and seen their circumstances change due to the effects of the pandemic. This is for businesses affected by COVID-19 outside the retail, hospitality, and leisure sectors. The government states that retail, hospitality and leisure businesses have not been paying any rates during the pandemic, as part of a 15 month-long relief which runs to the end of June this year, and are therefore excluded.
5. The £1.5 billion pot will be distributed according to official data on which sectors have suffered most economically, rather than on the basis of falls in property values.
6. This relief is an alternative to any adjustments to rateable values as a result of the change in circumstances.

Some Issues

- 7 Inevitably, this will have some criteria and there will be disputes and appeals. There are bound to be additional administrative and IT costs for local councils, but I can't see anything about the additional financial support for local councils for implementing the scheme. Will local council be expected to bear that cost? If so, this will impact on local ratepayers and services.
- 8 The government must bear the full cost of administering the scheme.
- 9 The basis of the £1.5 billion calculation is not known and how this will be disbursed. What will happen if the fund is exhausted? Will the government provide additional funding or will the local council be expected to top it up?
- 10 The income of individuals and families is also negatively affected by Covid-19 too. But there is no equivalent support for them. Why not?

INSOLVENCY

The second part of the Bill deals with insolvency abuses.

³ <https://www.gov.uk/government/news/business-rates-relief-boosted-with-new-15-billion-pot>

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11. The Company Directors Disqualification Act 1986 (CDDA) grants the Government powers to investigate the conduct of directors of insolvent companies by requiring the provision of information and documents.
12. It also allows the Insolvency Service to apply for a court order (or seek a disqualification undertaking) disqualifying a director who engaged in misconduct from serving as a director for up to 15 years⁵. However, because of what the Government considers to be a loophole, these powers in CDDA do not extend to former directors of dissolved companies. Investigating the conduct of directors of dissolved companies is currently a complex process requiring a court order to restore the company to the register.
13. In August 2018, the government issued a consultation paper⁶ to reform insolvency law and the Bill now follows its recommendations.
14. Under the Bill, if the Insolvency Service is satisfied that the conduct of a director of a dissolved company demonstrates that the director is unfit to be concerned in the management of a company, it can seek a disqualification order against that director, without first needing to restore the company.
15. A key point to note is that the Bill is intended to have retrospective effect i.e. the Insolvency Service could exercise the powers in relation to companies that were dissolved prior to the legislation coming into force.
16. The explanatory notes⁷ accompanying the Bill suggest that part of the rationale appears to be that the UK Government wants to target individuals who have inappropriately wound up companies after receiving Bounce Back Loans (presumably having used those loans for the directors' personal benefit) designed to enable smaller companies to survive the COVID-19 pandemic.

The impact assessment⁸ notes that the “extent of Bounce Back Loan fraud is highly uncertain, fraud losses¹⁸ are likely to be significantly above the general estimates of public sector fraud levels of 0.5% to 5% and up to 2.3% of approved applications were estimated to be duplicates”. It does not specify any amounts.

17. The government also appears to be concerned that directors of insolvent entities are using the dissolution process as a way of avoiding the cost and scrutiny which may come as a result of a formal insolvency process e.g. through liquidators and creditors⁹.

⁵ <https://www.gov.uk/company-director-disqualification>

⁶ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/736163/ICG_-_Government_response_doc_-_24_Aug_clean_version__with_Minister_s_photo_and_signature__AC.pdf

⁷ <https://bills.parliament.uk/publications/41476/documents/203>

⁸ [https://publications.parliament.uk/pa/bills/cbill/58-02/0011/Directors%20disqualification%20\(dissolved%20companies\)%20IA.pdf](https://publications.parliament.uk/pa/bills/cbill/58-02/0011/Directors%20disqualification%20(dissolved%20companies)%20IA.pdf)

⁹ <https://www.gov.uk/government/news/new-powers-to-tackle-unfit-directors-of-dissolved-companies>

18. The explanatory notes also suggest that the Bill seeks to tackle phoenixism, whereby directors cause or allow a company to be dissolved with a view to shedding liabilities, only to then incorporate a new company continuing the old company's business, free of those liabilities.

19. The impact assessment accompanying the report says:

The evidence shows 529,680 companies were dissolved in the UK during 2019¹¹ but a number of complaints were received (92 between February 2018 and December 2020) and just 33 were restored in England and Wales for the purposes of winding up via court order. Therefore, an estimate on the extent of abuse can be calculated as the number of complaints per year¹² divided by the number of dissolutions per year (32/529,680) which is 0.01% of dissolved companies.

20. The government has little or no financial data about the problem.

Lord Sikka (14 January 2021) to ask Her Majesty's Government how much unsecured creditors have been unable to recover from the bankruptcy of their corporate customers in each of the last five years¹⁰.

Lord Callanan (28 January 2021): This information is not collated and held centrally. Information on individual corporate insolvencies at Companies House contains reports filed by the appointed insolvency office holder which will detail the amounts owed to different types of creditors, including unsecured creditors, and any payments made to those creditors from the realisation of assets during the course of the insolvency process.

The full UK losses to creditors because of liability dumping through dissolution of companies are not known though the impact assessment¹¹ accompanying the Bill provides some snippets of information

- a) Between April and June 2016 there were 207 cases where an Employment award was made by the Tribunal but not paid by the employer and of these 7% (16) were not pursued by the penalties team as the company was dissolved.
- b) The Home Office have informed the Insolvency Service of 361 dissolved companies where debts of £5.7m were written off between February 2014 and October 2016, accounting for 45% of total debt write off (£11.8m).
- c) Trading Standards have provided anecdotal evidence that voluntary strike-off is being used to avoid payment of business rates.
- d) The impact assessment asserts that "Tax losses could be substantial", but does not provide an estimate. Instead it cites Australian evidence – " the

¹⁰ <https://questions-statements.parliament.uk/written-questions/detail/2021-01-14/HL12173>

¹¹ <https://publications.parliament.uk/pa/bills/cbill/58->

[02/0011/Directors%20disqualification%20\(dissolved%20companies\)%20IA.pdf](https://publications.parliament.uk/pa/bills/cbill/58-02/0011/Directors%20disqualification%20(dissolved%20companies)%20IA.pdf)

Australian Tax Office has estimated that Phoenix activity costs their exchequer around AUS\$600m a year”.

21. The Local Council Association¹² estimates that some £250 million of business rates are avoided through a variety of avoidance techniques.

Some Issues

22. How far back will the Insolvency Service go? The government should be probed. What additional funding will be given to the Insolvency Service?
23. The Insolvency Services is not that efficient. Carillion collapsed in January 2018 and hardly any of its directors have been disqualified. Speedy action against rogue directors is needed and the Insolvency Service is too slow.
24. This Bill is not preceded by any changes to the formation of companies. Currently, anyone from anywhere in the world can form a limited liability company in the UK¹³. There is no authentication check on the identity of individuals forming the company, or its directors or shareholders. UK registered companies have some 6.8 million directors¹⁴. How many are resident outside the UK or are bodies corporate is not known. So there are major questions about the enforcement of the Bill.

Companies House acts more like a filing box and rarely performs any meaningful checks. Thousands of UK companies have directors whose addresses are in secretive offshore jurisdictions¹⁵. It is impossible for the UK to call foreign nationals to account for corporate malpractices. How will the government prosecute these individuals? Will it end up disqualifying phantom directors?

25. To take action, the government needs to be able to identify the parties behind shell companies, but this is not possible in the UK as company law permits nominee shareholdings i.e. enables concealment of the identity of the real beneficiaries. No reform is proposed. Why not?
26. Private companies in the UK need one director who must be a natural person. However, the government states¹⁶ “Directors do not have to live in the UK but companies must have a UK registered office address”. So how will the government enforce the proposed law against foreign nationals?
27. The government does not take any action against false filing of information by individuals resident abroad

¹²<https://www.local.gov.uk/sites/default/files/documents/5.70%20Business%20rates%20avoidance%20survey.pdf>

¹³ <https://publications.parliament.uk/pa/cm201719/cmpublic/sanctions/memo/SAMLB07.pdf>

¹⁴ [https://publications.parliament.uk/pa/bills/cbill/58-02/0011/Directors%20disqualification%20\(dissolved%20companies\)%20IA.pdf](https://publications.parliament.uk/pa/bills/cbill/58-02/0011/Directors%20disqualification%20(dissolved%20companies)%20IA.pdf)

¹⁵ <https://www.theguardian.com/uk/datablog/2013/apr/03/uk-companies-controlled-offshore>

¹⁶ <https://www.gov.uk/limited-company-formation/appoint-directors-and-company-secretaries>

Kelvin Hopkins (Luton North) on 14 September 2017¹⁷: To ask the Secretary of State for Business, Energy and Industrial Strategy, whether any action has been taken against the promoters and officers of Magnolia Fundaction UK Ltd for filing information at Companies House which stated a director's name as The Chicken Thief and described his occupation as fraudster.

Answered by Margot James on 12 October 2017: No action has been taken at this time against the promoters and officers of Magnolia Fundaction UK Ltd for filing inappropriate information in Italian at Companies House.

So how will it implement the proposed legislation?

28. Public limited companies, as defined in the Companies Act 2006, must have at least two directors. One of these can be a legal person i.e. another companies.

These corporate directors can be registered in secretive tax havens where nothing is publicly known about shareholders or directors of the companies. The registered address is about the only publicly available information.

Ugland House in the Cayman Islands, a UK overseas territory, is the registered address of 40,000 business entities¹⁸. The identity of their directors is not known. Therefore, it is impossible to disqualify anyone.

The British Virgin Islands¹⁹, another UK overseas territory, has 30 registered companies per head of population and little is known about them or their controllers but they can become directors of UK PLCs.

These companies rarely carry out any trade in their locales, but facilitate secrecy to their owners, an ingredient necessary for frauds and illicit flight of capital. So again, how will the UK government enforce its laws against foreign legal persons whose identity may not even be known?

29. One consequence/danger of the proposed legislation is that directors dissolving companies, because it is cheaper, may automatically be construed as unfit and leave those involved, whether actual named directors or "de facto" directors, open to disqualification.

30. How will the Insolvency Service know that a company has been dissolved? Will it monitor companies House filings? The Bill does not say anything.

31. The proposed regime for dissolved companies will suffer from the same problem as the current regime for live companies: the requirement that an interested party, most likely a creditor, raises concerns about the conduct of the company's directors with the Insolvency Service. While directors are required to notify the actual, contingent and prospective creditors of a company of that company's proposed dissolution, and such creditors have an opportunity to object to the

¹⁷ <https://questions-statements.parliament.uk/written-questions/detail/2017-09-14/105290>

¹⁸ https://en.wikipedia.org/wiki/Ugland_House

¹⁹ https://en.wikipedia.org/wiki/British_Virgin_Islands_company_law

proposed dissolution before it takes effect, not all such creditors may be notified in practice (if, for example, certain creditors were unknown to the directors or if the directors don't follow the proper process). Once a company has been dissolved, there is no equivalent of a liquidator or an administrator of an insolvent company, who has a duty to investigate the conduct of directors and directors and report to the Insolvency Service. This makes it more likely that only particularly egregious examples of misconduct, significant enough to come to the attention of an interested party, will be investigated in respect of directors of dissolved companies.

32. But companies can also be dissolved in other ways. For example, Companies House can take steps to dissolve a company if it fails to file annual accounts within the specified time limits. So will rogue directors choose this method, which does not seem to be covered by the Bill?
33. The government says that 2.3% of approved applications for Bounce Back Loans are likely to be duplicates or fraudulent. This begs questions about the diligence checks in handing out monies, especially as anyone from anywhere in the world can form a company in the UK.