

SUMMARY: INTERVENTION & OPTIONS

Business Enterprise and Regulatory Reform	Impact Assessment of The Companies (Reduction of Share Capital) Order 2008
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Stage Final 23/4	Version one	Related Publications: Implementation of Companies Act 2006 Consultative Document February 2007 http://www.dti.gov.uk/consultations/page37980.html
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Available to view or download at: [www](http://www.dti.gov.uk/consultations/page37980.html).

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What is the problem under consideration? Why is government intervention necessary?

There are two issues.

1. The need to prescribe the form in which a solvency statement must be made when a private company proposes to reduce its share capital when relying on the statement without getting a court order; and
2. The need to provide that when a company reduces its share capital, and the reduction has been confirmed by a court order, subject to three exceptions, the reduction is distributable unless the court orders that it is not.

Government intervention

Under Company Law there is no minimum capital requirement for private companies but there are restrictions on how capital invested in a company is subsequently treated. The restrictions reduce the likelihood of shareholders – who are protected through the mechanism of limited liability - behaving in an opportunistic manner, which might, ultimately, be at the expense of creditors or possibly minority shareholders. The use of the court route method, and now the option of a solvency statement, for any capital reductions enables creditors to take comfort from capital invested in the company whilst also providing flexibility for the directors of the company to manage the business efficiently and return unused capital appropriately.

What are the policy objectives of the Regulations and their intended effects?

The objectives are

- (i) to prescribe the form in which a solvency statement must be made; the content is dictated by Companies Act 2006 section 643. The Registrar of Companies will also have powers to impose, via Companies House rules, requirements relating to the form, manner of delivery and authentication of the copy of the solvency statement, which will need to be registered at Companies House.
- (ii) to provide for the treatment of reserves arising from reduction in share capital including where a solvency statement has been used to reduce share capital; and to end reliance on professional guidance in these matters

The intended effects are

- to provide a simplified and non-court mechanism by which a private company can reduce its share capital, which is cheaper and has a lighter legislative touch.
- to clarify the treatment of reserves arising from a reduction of share capital in all circumstances (including where the new solvency statement has been used) and to make the treatment of reserves a matter of legislation rather than one of professional guidance.

The introduction of the solvency statement route and the clarification of treatment of reserves arising from share capital reductions is viewed as effect neutral for creditors.

What policy options have been considered? Please justify any preferred option.

Capital Reduction by private companies using solvency statement – under the Companies Act 1985 capital reduction for both private and public companies requires court confirmation. The Company Law Review recommended a non-court route for capital reduction by private companies. Consequently the policy option that existed was to introduce a non-court procedure for private companies to reduce share capital or not to introduce it: business welcomes its introduction.

Distributions – the treatment of reserves arising from reductions in share capital is currently subject to the provisions of the Companies Act 1985 and lengthy, and complex, professional guidance issued by the Institute of Chartered Accountants in England and Wales (ICAEW). Under the Companies Act 2006 the policy options were to replicate what existed under the Companies Act 1985 thereby continuing reliance on the professional guidance or setting out in legislation, by means of secondary legislation provided for by the 2006 Act, how such reserves were to be treated. Key stakeholders, the ICAEW, supported by the Law Society, favoured setting the treatment of reserves in legislation and that was the policy option adopted.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

3 – 5 years

Ministerial Sign-off:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options

Signed by the responsible Minister:

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Signed by the responsible Minister:

Date:

SUMMARY: ANALYSIS & EVIDENCE

Policy Option :				
ANNUAL COSTS		See "Costs and Benefits" in Evidence Base below		
One off (Transition)	<input type="text" value="nil"/>	Yrs	<input type="text"/>	
Average Annual Cost (excluding one-off)		<input type="text"/>		
Other key non-monetised costs				
ANNUAL BENEFITS		See "Costs and Benefits" in Evidence Base below		
One off	<input type="text"/>	Yrs	<input type="text"/>	
Average Annual Benefit (excluding one-off)		<input type="text"/>		
Other key non-monetised BENEFITS		Total Benefit PV <input type="text"/>		
Other key non-monetised BENEFITS				
KEY Assumption/Sensitivities Risks				
Price Base Year	Time Period Years	Net Benefit Range (NPV) £-£	NET BENEFIT (NPV Best Estimate) £	
What is the geographic coverage of the policy/option?		UK		
On what date will the policy be implemented?		1 October 2008		
Which organisation(s) will enforce the policy?		Companies House		
What is the total annual cost of enforcement for these organisations?		nil		
Will implementation go beyond minimum EU requirements		no		
What is the value of the proposed offsetting measure per year?		n/a		
What is the value of changes in green gas emissions?		n/a		
Will the proposal have a significant impact on competition?		no		
Annual cost per organisation (excluding one-off)		Micro 0	Small 0	Med 0
Are any of these organisations exempt?		No	No	No
Impact on Admin Burdens Baseline (2005 prices)				
Increase of	<input type="text"/>	Decrease of	<input type="text"/>	Net Impact <input type="text"/>

Evidence Base for Summary Sheets

Background

1. A consultation exercise was conducted between February and May 2007 on secondary legislation to be made under the Companies Act 2006. Draft regulations were published on the department's website in May 2007 for comment, including provisions relating to the new solvency statement route for capital reduction. Although the draft Companies (Reduction of Share Capital) Order 2008 is not identical to the draft regulations published in May 2007, the substance of the Order is essentially the same as the substance of the equivalent provisions in those draft Regulations and is a consequence of that consultation exercise and subsequent contributions from stakeholders.
2. Under the Companies Act 1985 the treatment of reserves arising from a reduction of share capital has been governed by professional guidance issued by the Institute of Chartered Accountants in England and Wales (ICAEW). The guidance is long and complex, and representations were made by the ICAEW and the Law Society (LS), that the opportunity should be taken to clarify the treatment of such reserves in legislation. We have consulted at length with both the ICAEW and LS to achieve an agreed draft Companies (Reduction of Share Capital) Order and we now wish to secure wider acceptance by placing the same on the departmental website, for information and views, for a period of four weeks.
3. On 1 October 2008 provisions of the Companies Act 2006 will be commenced enabling private limited companies to reduce their share capital by means of a new procedure, the solvency statement route, which will not require court involvement. Currently both public and private limited companies must have a reduction of share capital confirmed by court order.
4. Traditionally companies limited by shares have been seen as a mechanism by which the owners – shareholders – limit how much of their money is at stake and this money can only be returned to shareholders in certain circumstances. For many private companies the existing framework for return of capital is unnecessarily complicated and its simplification offers a beneficial deregulatory outcome.
5. The changes are permissive and in the majority of cases there are no obvious costs; we anticipate that any costs to a company that arise will be marginal and that they will be more than offset by the cost savings that flow from the deregulatory measure in question.
6. It is clear that the measures in the 2006 Act will save companies both time and money as they will be able to avoid the necessity of going to court to restructure its share capital i.e. in the case of capital reductions by private companies. Under the Companies Act 1985 the procedure for reducing share capital for both private and public companies involves confirmation by a court, which can be both time-

consuming and expensive. The change in legislation – to introduce for private companies a non-court route for reducing capital – requires government action.

7. Where there has been a reduction of share capital the Order provides clarity as to the treatment of any reserves arising from that reduction. Furthermore there is a strong element of creditor protection in that where a limited company reduces its share capital it must put that reduction through its profit and loss account (so diminishing or cancelling losses on that account) before the funds become available for distribution to shareholders.

Costs and benefits

8. There is no data on the sums companies expend in complying with the relevant Companies Act 1985 legislation and consequently we are unable to calculate the financial costs or benefits that will arise from the proposed changes. We have however taken informal soundings from stakeholders and we are content that in relation to the introduction of the solvency statement procedure
 - only minimal costs to private companies may arise from having to complete forms and registering them at Companies House;
9. Benefit will accrue from matters including:
 - not having to ‘settle’ a list of creditors as is required in the court procedure,
 - not having to put into place arrangements to satisfy the court that debts are provided for, and
 - not having to fund professional advisors to ensure these matters are undertaken appropriately via the courts
10. We are unaware of any significant costs arising to Companies House from the introduction of this procedure.
11. The Courts will benefit from not having to confirm reductions of share capital for private companies in every case.
12. Matters relating to the clarification of treatment of any reserves arising from a reduction of share capital, i.e. distribution, do not have obvious mandatory costs.

Available sanctions

13. The available sanctions need to be understood in context; as the balance to providing a reduced burden on companies and greater flexibility for company directors.
14. If the directors make a solvency statement without having reasonable grounds for the opinions expressed in it, and the statement is delivered to the registrar of companies every director who is in default will be guilty of an offence punishable by a fine or up to two years imprisonment. We do not believe that directors will be “put off” from using the solvency statement route because the sanction is available. Informal feedback suggests that the solvency statement route is being widely anticipated and we understand companies are currently deferring court route applications preferring instead to wait until post-October 2008 so that they can take advantage of the solvency statement route.

15. There is no requirement for directors to obtain professional advice when making a solvency statement. Directors are the stewards of their companies and therefore aware of the trading and financial status; if they seek professional advice that is a matter for them. There is no basis to support a view that benefits accrued will be reduced by directors seeking professional advice.

Mandatory Impact Tests

16. We have considered the three mandatory impact tests (gender, race, disability) and the recommended options are unlikely to have any discriminatory effects.

Specific Impact Tests - Checklist

Type of testing undertaken	Results in Evidence Base? (Y/N)	Results annexed? (Y/N)
Competition Assessment	n/a	
Small Firms Impact Test	n/a	
Legal Aid	n/a	
Sustainable Development	n/a	
Carbon Assessment	n/a	
Other Environment	n/a	
Health	n/a	
Race Equality	y	
Disability Equality	y	
Gender Equality	y	
Human Rights	n	
Rural Proofing	n/a	