The Taxing Wealth Report 2024

Every politician's guide to "How to pay for it"[1]

The reform of tax administration:

Reforming the administration of Companies House

Brief Summary

This note proposes that:

- Companies House is an almost wholly ineffective regulator of limited liability companies in the UK, many of which might be used to facilitate tax abuse and fraud.
- This is profound concern to the operation of markets in the UK, most especially when there are more companies incorporated in the UK each year than there are live births.
- There are numerous reasons for this failure on the part of Companies House, including:
  - The ease with which companies can be incorporated without proof of the identity of those doing so necessarily being required.
  - The incredibly cheap regulatory fees payable in the UK, which deny resources to Companies House to regulate companies.

[1] This note forms a part of 'The Taxing Wealth Report 2024' published by Finance for the Future LLP, which is UK LLP number OC329502, registered at 33 Kingsley Walk, Ely, Cambridgeshire, CB6 3BZ. See https://www.financeforthefuture.com/taxing-wealth/. This note was written by Richard Murphy FAcSS FCA FAIA (Hon), Professor of Accounting Practice, Sheffield University Management School, who is a director of Finance for the Future LLP. © Finance for the Future LLP 2023

The Taxing Wealth Report 2024 is a joint project between:

Finance for the Future and Sheffield University Management School

  - The failure of Companies House to require accounts complying with either company law or accounting standards on public record, and their failure to address failures in this regard when they are drawn to their attention.
  - The lax attitude that Companies House has towards the striking off of companies from the register that they maintain when companies are in default of their legal obligations, which failure on their part facilitates the use of limited liability companies by fraudsters, whether with regard to tax or otherwise.
  - The failure of Companies House to prosecute in the case of most corporate failures to provide information that should be submitted to them by law.
- The cost of this failure in terms of tax lost and in terms of fraud facilitated cannot be known, but when the former is conservatively estimated to cost £19 billion a year and the latter has been estimated to have a further cost to the government exceeding £30 billion per annum and to the private sector of in excess of £150 billion per annum[2] the scale of abuse facilitated by almost wholly unregulated limited liability companies within the UK economy is so large that it is hard to avoid the conclusion that Companies House is the facilitator of a criminogenic environment within the UK economy, even if inadvertently.
- To address this issue a series of radical reforms are proposed including:
  - Annual checks on the identities of all directors and significant shareholders involved with UK companies.
  - A requirement that UK companies have a share capital commensurate to their level of trading and that shareholders should have unlimited liability to the extent that this capital is not made available by them.
  - That the full details of all directors of a company should be available to Companies House on all occasions and should be on public record unless a case for withholding information can be proven.
  - That the full trading addresses from which the company operates should be recorded on public record.
  - That the full accounts of all companies as due to its shareholders should always be available on public record.
  - That the directors and principal shareholders of a company that is dissolved without filing full accounts to the time when application for dissolution is made, including a creditors list, shall lose the right to limited liability with regard to any debts owing at that time.
- That although the Taxing Wealth Report 2024 has already estimated that maybe £6 billion of additional tax might be collected a year as a result of tackling

[2] https://issuu.com/petersandpeters.com/docs/annual_fraud_indicator_report_2023

deficiencies in the administration of the UK's corporation tax system a further similar sum might be raised by these proposals because of the limitations in other frauds that they might facilitate.

- The cost of these extra safeguards should be covered by increasing the currently minimal fees charged by Companies House.

The proposal	To reform the administration and enforcement regimes of the UK's Companies House and to require the supply of additional data concerning the commercial activity of companies to Companies House by the UK's commercial banks and others in the UK's financial services sector.
Reason for the proposal	1. To reduce the risk of the abuse of limited liability status to avoid and evade taxation obligations and other regulatory obligations. 2. To reduce tax gaps, and so increase tax paid by those with wealth in the UK who take most advantage the opportunities provided by the incorporation of companies within the UK. 3. To increase the effectiveness of resource usage by HM Revenue & Customs in the management of tax risk arising from the operation of limited liability companies. 4. To improve taxpayer accountability and compliance, most especially with regard to the use of limited liability entities. 5. To increase horizontal tax equity, which can be undermined by the abuse of limited liability companies. 6. To increase vertical tax equity, which can be undermined by the use of limited liability companies by those with wealth.

	7. To help close the tax evasion and tax avoidance tax gaps. 8. To reduce the tax spillover effect that existing arrangements fort the regulation of companies in the UK create. 9. To raise additional tax revenues.
Estimated tax that might be raised as a result of the recommendation made	The behavioural response to this recommendation cannot be known, although it is likely to be significant, which is why it is being made. The amount of tax abuse, including tax evasion, that is being undertaken as a result of the abuse of limited liability companies cannot be known, but is likely to be very significant for reasons noted below. HM Revenue & Customs estimate the tax loss to be at least £19 billion per annum[3]. Other fraud against the government might exceed £30 billion per annum, of which at least half might well be committed by limited liability companies. In the private sector economy fraud might exceed £150 billion per annum, which will in turn contribute to the UK tax gap, which may well be much bigger than HM Revenue & Customs estimate because of limitations in the methods that they use to estimate that figure as noted elsewhere in the Taxing Wealth Report 2024. Not all of this will be facilitated by those using limited liability companies, but a significant part will be. Reducing the abuse of limited liability companies to prevent the accumulation of untaxed wealth must be a significant objective of any programme with regard to the taxation of wealth.

[3] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1164246/Measuring_tax_gap_online_tables_2023.xlsx table 7.1 interpreted by author.

	Unlike almost all the other recommendations made in the Report of which this note forms a part, the issue addressed here focuses on tax evasion and unpaid tax. When HM Revenue & Customs estimate that 56 per cent of the tax gap relates to the activities of smaller business, most of which will be operated via limited liability companies, the scope for tax recovery as a result of the enhanced regulation of limited liability companies amounts to many billions of pounds per annum[4]. This is most especially the case when it is considered likely that the majority of tax abuse in the UK is undertaken through the medium of private limited companies.
Ease of implementation	The changes proposed will take some time to implement and will require the expenditure of significant political capital by a government seeking to implement the proposed changes since opposition to them is likely to be significant. The costs of the proposed changes can easily be covered by increasing the current exceptionally low fees charged by Companies House, where the annual fee for maintaining a company is currently no more than £13 a year in most cases.
Likely difficulties that might result from implementation	As noted above, there is likely to be significant opposition to these changes although they should be relatively easy to legislate and implement at a technical level.
Likely time required to implement the change	A process likely to take a number of years.
Consultation period required.	At least a year as opposition is likely and will have to be noted.

[4] Table 1.4 interpreted by author from https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1164246/Measuring_tax_gap_online_tables_2023.xlsx

Introduction

Companies have existed in the UK since the 15th century. Most early companies were associated with the exploitation of monopolies. As such they have been linked to economic abuse for as long as they have existed. The East India Company is an example of one such early entity.

In the UK the company as we now know it is associated with the growth of industry, starting with the development of canal companies in the eighteenth and early nineteenth centuries. The popularity of incorporation grew with the rise of railways in the early nineteenth century. These companies from the early industrial era were incorporated by separate acts of parliament. The Joint Stock Companies Act 1844 first permitted incorporation by registration. From 1855 this was possible with limited liability. As a consequence, the modern company that exists because of its registration by the UK Registrar of Companies (now usually known as Companies House) was born.

In March 2023[5]:

- The total UK company register recorded the existence of 5,116,743 companies, an increase of 4.5% compared with March 2022.
- There were 801,006 company incorporations in the year ending March 2023, an increase of 6.4% compared with the previous financial year.
- In that same year there were 585,807 dissolutions, an increase of 0.7% compared with the previous year.
- The average age of a company on the register at the end of March 2023 was 8.6 years.
- Private limited companies accounted for over 95% of all companies on the register.

To put these figures in context, there were 605,479 live births in England and Wales[6] in 2022. Whilst the figures for companies cover the whole UK, what is apparent is that there

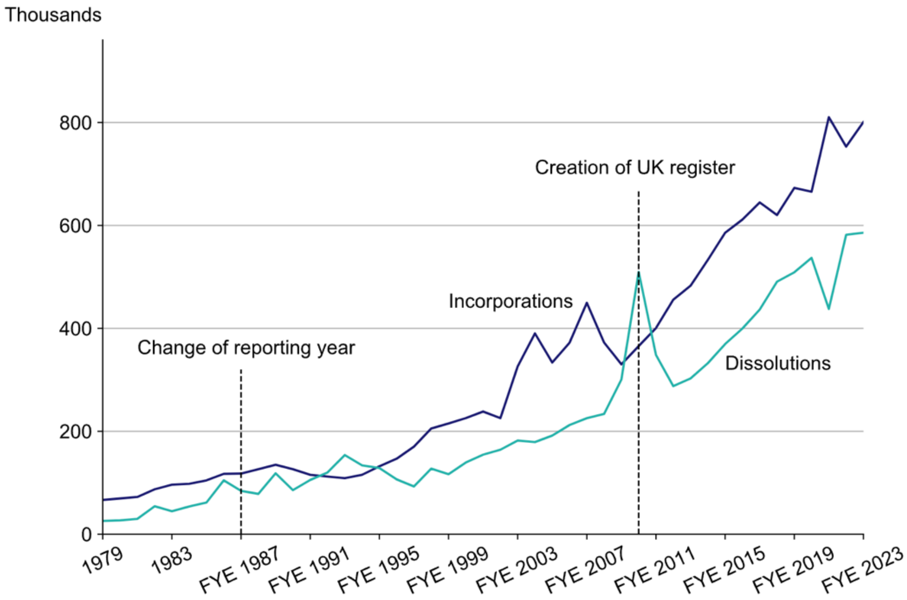
[5] Data from https://www.gov.uk/government/statistics/companies-register-activities-statistical-release-2022-to-2023/companies-register-activities-2022-to-2023

[6] https://www.ons.gov.uk/peoplepopulationandcommunity/birthsdeathsandmarriages/livebirths/bulletins/birthsummarytablesenglandandwales/2022#:~:text=3.-,Live%20births,compared%20with%202021%20(624%2C828).

are more companies created in the UK at present than there are live births. Thankfully, the life expectancy of children is longer.

The growth in the number of companies is demonstrated by this chart published by the UK's Companies House[7]:

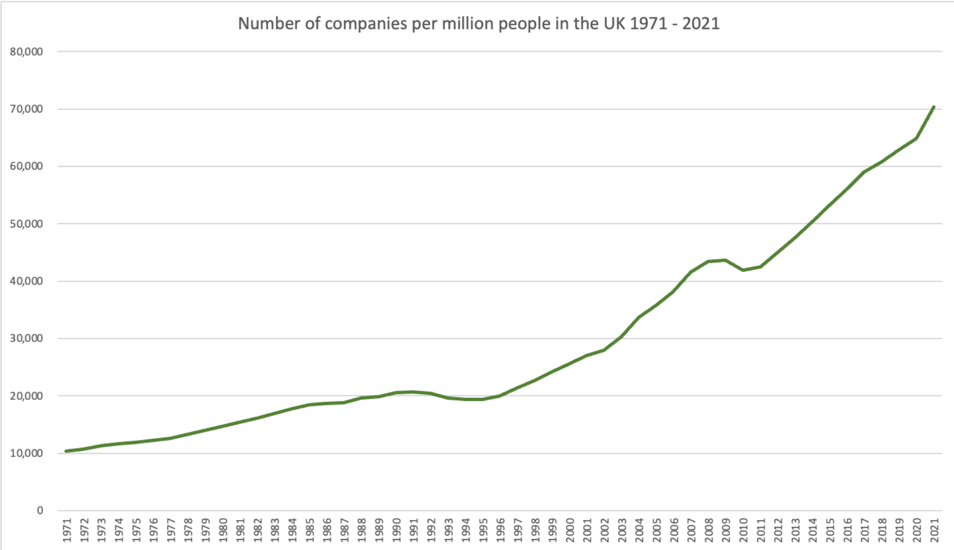
Incorporations and dissolutions, UK companies register, 1979 to FYE 2023. "Creation of UK register" refers to the merging of the Great Britain and Northern Ireland registers



Source: Companies register activities FYE 2023, Companies House

To put these figures in context, this chart shows that the number of companies per head of population grew seven-fold between 1971 and 2021:

[7] https://www.gov.uk/government/statistics/companies-register-activities-statistical-release-2022-to-2023/companies-register-activities-2022-to-2023



Sources: Companies House[8], the Office for National Statistics[9] and author's calculations

As is apparent, the growth in company numbers has been extraordinary. Several phenomena have contributed to this:

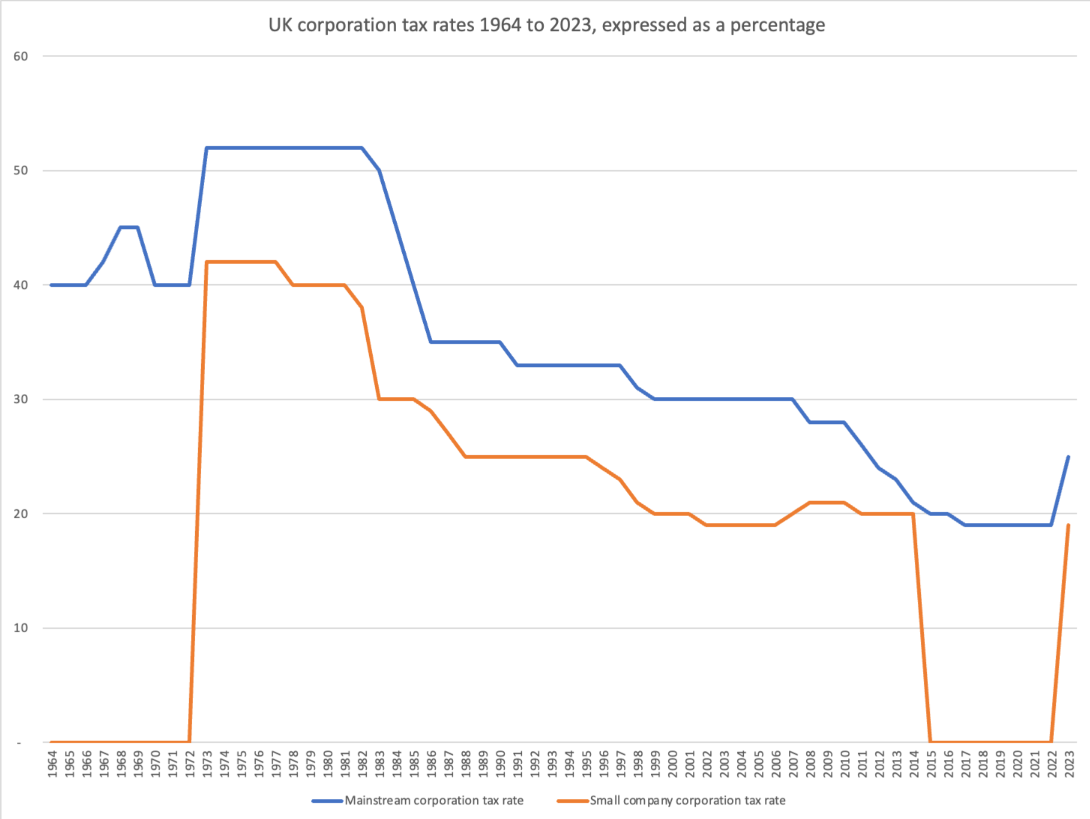
- The relaxation of audit requirements for most companies during the 1990s, so that in this century fewer than five per cent of companies require an audit, significantly reducing the cost of managing a company.

- Since the audit requirements on limited companies were removed there have been no quality control checks on the accounts filed by UK limited companies. Companies House is specifically a registrar of companies, and not a regulator of them. Accounts bearing little or no relationship to the requirements of company law can be, and are, filed at Companies House without comment from them arising. The checks that they perform are decidedly limited e.g., the company number on the accounts must be correct; as must the date be appropriate; the accounts must be signed (at least electronically); and the balance sheet must balance. It seems that few other checks are made and complaints on deficient accounts are rarely addressed. As such there is no effective regulation of UK accounting law.

- The significant reduction in corporation tax rates over time, demonstrated by this chart:

[8] Table A8 at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1165559/Companies_Register_Activities_FYE_2023.xlsx

[9] https://www.ons.gov.uk/peoplepopulationandcommunity/populationandmigration/populationestimates/timeseries/ukpop/pop



Sources: Author's accumulated data sources

As is apparent, the rate of corporation tax has fallen considerably, and most especially since the mid 1990s, since when the use of companies has increased considerably.

Note that when no small company tax rate is shown it is the same as that for large companies. Large is defined by profits, not the scale of a company's activities, with the cut off changing over the period noted.

It will be noted that in some recent years the rate of corporation tax has, for all companies, been lower than the basic twenty per cent income tax rate.

- The ease of incorporation of companies in the UK. The UK is now notorious for this ease, based on these facts:
  - It usually costs just £12 to form a company in the UK[10].
  - Those incorporating a company in the UK still do not need to prove their identity for money laundering purposes.

[10] https://www.gov.uk/government/publications/companies-house-fees/companies-house-fees

  - The annual recurring registration fee for a company is £13.

  - The fee to have a company voluntarily struck off the UK register of companies is £8.

  - No evidence of the identity of newly appointed directors or major shareholders is required.

  Legislation before parliament at the time of writing may require that proof of identity might be required by Companies House in the future and that some fees will increase as a result, but the move still leaves the UK well behind other countries when it comes to the regulation and control of new company creation.

  Not surprisingly, this fact has been noticed by many outside the UK. UK company formation agents have often marketed their services to persons outside the UK, including to Russians until recently.

- UK companies can be disposed of with ease:

  - In the year to March 2023 there were 585,807 companies dissolved in the UK[11].

  - Of this number 557,096 were 'struck off' the register of companies i.e. they were dissolved either because the company applied for this to happen, suggesting in the process that they had no liabilities owing (to secure which striking off they pay a fee of £8), or they were removed by Companies House because of the company's failure to file either an annual confirmation statement or annual accounts. The remainder (28,711, or 4.9 per cent of the total) were formally dissolved as required by company law.

  - Companies House do not provide an analysis within their statistics of the number of companies dissolved at their own choice and the number struck off by Companies House for failing to comply with regulatory requirements. When the author of this note last investigated this issue[12] in 2014, around 45 per cent of all companies struck off the register were removed by Companies as a result of a company's failure to supply documentation required by law. Assuming that the ratio remains the same now, around 250,000 companies a

[11] https://www.gov.uk/government/statistics/companies-register-activities-statistical-release-2022-to-2023/companies-register-activities-2022-to-2023

[12] http://www.taxresearch.org.uk/Documents/Intheshade.pdf

year might be removed from the register each year because of their failure to comply with regulatory requirements.

The ease with which UK companies can be disposed of with few, if any, questions being asked compounds the problems created by the absence of any effective company law enforcement regime with regard to accounting and creates a criminogenic environment in the UK which some can use to facilitate the abusive accumulation of wealth. This is why this matter requires action.

Recommendations

The key problems being faced as far as the regulation of Companies House, company law and tax are concerned are:

- Not knowing who owns and manages companies and which people are, therefore, responsible for taxes payable.

- The ease with which companies can be created and dissolved very often with no data of any sort with regard to their activities being filed with any relevant authority, including HM Revenue & Customs, which might permit the illicit accumulation of wealth.

- The absence of any quality control data over accounts filed by limited companies.

- The ability that companies have to avoid settlement of their tax liabilities, a fact exacerbated by the fact that HM Revenue & Customs is very often one of the largest creditors of failing companies as a result of the deliberate choices made by their directors, who might profit from this decision.

There are also matters relating to other frauds to consider, abating which might also raise tax revenues.

The recommendations that follow are meant to address these issues.

1. The identity of all company directors and persons controlling more than ten per cent of a company should be proved to Companies House by each company annually. The creation of registers of those holding such positions that could be updated for all appointments and shareholdings simultaneously would mean this should not be an onerous obligation. Linking this register to passport and driving licence data would make the process even easier and more reliable. The opportunity to save tax anonymously should be abolished.

2. Companies should have a share capital commensurate to their level of trading and those not doing so should be able to call on their shareholders to make good the deficiency in the event of an insolvency. Shareholding cannot be seen to be a risk-free activity when it clearly is not. This should mitigate the tax losses arising to HM Revenue & Customs annually as a result of unpaid tax.

3. All company accounts should be available on public record, in full, and accounting standards should ensure that they are designed to meet all shareholder needs[13].

4. Companies failing to file accounts on time should lose the benefit of limited liability until they do so.

5. Details of all directors and shareholders should be on public record. Those companies not filing correct data should lose their limited liability. Exceptions should only be made in the case of proven risk.

6. A full list of the trading addresses of all companies should be available on public record.

7. All companies must be required to file tax returns annually (many do not at present). Those that do not should have personal liability imposed on the directors for tax owing. For more information on this issue refer to the Taxing Wealth Report 2024 note on corporation tax administrative reform.

8. No company should be struck from the Register of Companies without filing accounts, including creditor lists, if insolvent. Failure to do so should result in unlimited liability for the debts of the company on the part of all its directors and principal shareholders (those holding more than 10 per cent of the equity). Failure to acknowledge any debt owing by the company should also result in unlimited liability to the unacknowledged creditor.

9. Banks must be required to share with Companies House and HMRC annually the details that they should on the company, its trading addresses, the shareholders and directors and must supply a figurine for sums deposited in all bank accounts that they holds for it. In the absence of company supplied data this information should be placed on company record in place of company supplied data. For more information on this issue refer to the Taxing Wealth Report 2024 note on corporation tax administrative reform.

[13] Note that proposals to achieve this goal are now being legislated

These measures will be seen as tough, and there will be protest from 'free marketeers'. However, limited liability, as Adam Smith knew and did not like, creates the chance for free-riding, moral hazard and straightforward abuse that undermines all theories of market competition. As such, any such protest cannot actually be about support for free markets. They would, therefore, be more like a defence of free-loading, because that is what limited liability has become, and what it will remain unless action to end abuse is taken.