

Mackrell

Corporate Law

Section 110 Reconstruction – Protecting Assets in an Uncertain Economy



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What is Section 110 Reconstruction?

One way a company can carry out a corporate demerger is by using the solvent voluntary liquidation route set out in Section 110 of the Insolvency Act 1986. A Section 110 Reconstruction involves the demerger of the business and assets of an existing company/group by transferring them to two or more newly formed companies in return for shares in the new companies.

What is the process?

In most cases, a new holding company (with no trade creditors or liabilities) will be used to make the process more straightforward. The steps involved are as follows:

1. A new holding company is formed.
2. Exchange of shares in the original parent company for shares in the new holding company (the 'demerging company').
3. The demerging company is placed into solvent voluntary liquidation and a liquidator is appointed.
4. The liquidator transfers the demerging company's assets to two or more new companies in exchange for shares in the new companies.
5. The liquidator distributes all of the assets owned by the new holding company (i.e. properties, trades, subsidiaries) to the original shareholders.
6. The demerging company is then dissolved.

Why use it?

A Section 110 Reconstruction is commonly used where shareholders wish to divide the assets of a business. This can be for a number of different reasons including:

- To separate valuable properties/assets from risky trades in order to better protect them from future unsecured creditors.
- Spinning out a trading venture from an existing company or group that could be sold at efficient Capital Gains Tax rates in due course.
- To simplify complex corporate group structures.
- Allowing shareholders to go their separate ways following a disagreement.
- Inheritance tax and succession planning.

Another advantage is that the demerging company doesn't need to have distributable reserves to effect a Section 110 Reorganisation (as no dividend is being paid).

What are the tax implications?

Reorganisations can lead to significant tax liabilities depending on the nature of the businesses and assets involved.

However, with careful tax planning and after obtaining a clearance from HMRC prior to the reorganisation, it is usually possible for these reconstructions to take place without giving rise to any significant tax liabilities.

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