The simple things in life

Bernadette Barber

As a business grows it becomes more and more complex, launching new ventures, spinning off subsidiaries and leaving them to gather dust when they outlive their purpose. Time for a spring clean, says Bernadette Barber.

The term 'less is more' may originally have been coined in relation to minimalist architectural styles, but it could equally apply to the complex corporate structures of many larger groups of companies. Cluttered with historical non-trading and dormant companies, many groups could benefit from a good old-fashioned clear-out.

It's easy enough to understand why groups accumulate a large number of inactive companies. Each new merger or acquisition seems to bring its own raft of subsidiaries, the histories and original purposes of which can be something of a mystery to those who inherit responsibility for them. And then there are the new business launches, joint ventures and tax efficiency initiatives, each one seemingly requiring one or more new companies – at least, that is, until they fall by the wayside, leaving those specially incorporated vehicles to gather dust.

As every company secretary knows, each of these companies adds a bit more to the annual compliance burden, and in an ideal world there would be time in one's busy diary to dissolve them. But with a 'to do' list full of urgent priorities, a housekeeping task such as getting rid of these unnecessary entities is rarely top of the agenda.

However with estimates placing the average cost of maintaining each dormant or inactive subsidiary within a larger group at several thousand pounds per year, maybe dissolving those redundant companies should be treated as a more pressing issue.

Mounting costs

A look at how those costs associated with dormant or inactive subsidiaries build up might convince even the most reluctant of businesses to take action.

Let's start with the company secretary's responsibilities. Now that annual returns can be filed electronically, each one only takes a few minutes to process and the reduced statutory fee of £15 per company is hardly going to break the bank. There is also the approval and filing of the annual report & accounts – even though, per company, this is not a major task, the aggregate effect in a large group can certainly be significant. Then there is the matter of occasional changes to the statutory registers, event-driven directors' and shareholders' resolutions, and filings to Companies House. Even with the efficiencies of modern company secretarial software and electronic filing, these tasks can account for a considerable amount of time.

In other words, the basic company secretarial administration of each company is time-consuming, and few would argue that it is the best use of a busy company secretary's time, especially when the companies in question are adding no value. That said, the time and resources needed to carry out the company secretary's responsibilities alone do not account for thousands of pounds per dormant subsidiary each year. So where else do costs build up?

The answer is, of course, that the company secretarial function is not the only in-house department spending time on these companies. The report and accounts need to be prepared elsewhere in the group, so there's the cost of the finance department's time to take into account. Then there is the board meeting for each company to approve its accounts, which takes up directors' valuable time as well as that of the company secretary.

The tax department, meanwhile, will no doubt also be busy with these redundant companies' tax computations, as well as dealing with issues such as transfer pricing which can often arise notwithstanding that a subsidiary is inactive. And, perhaps to a lesser extent, some other departments such as internal audit have to spend a certain amount of time on each company. The list just goes on and on.

Nor is the problem confined to internal costs. With each subsidiary's finances needing to be consolidated into the group results, the existence of unnecessary companies is certainly going to increase the duration and complexity of the group's already-expensive audit. And what about D&O insurance? By how much would its premium be reduced if there were fewer companies' directors and officers to cover?

And there can be indirect costs, too. Complex corporate structures are inherently risky and lack the transparency understandably preferred by regulators, rating agencies and investors alike. Can any business really afford to put unnecessary barriers in the way of finding favour with these third parties?

Thinking simple

At the risk of stating the obvious, then, the greater the number of subsidiaries within a group, the bigger the task of managing them will be.

Legislation also has a part to play here, especially the new Companies Act. The company secretaries of those groups which currently employ the mechanism of appointing a corporate director as sole director of their subsidiaries, will soon find themselves with multiple board vacancies to fill. When the Act puts an end to the use of sole corporate directors and forces companies to appoint at least one natural person to the office of director, some company secretaries will undoubtedly be faced with dozens of new vacant directorships.

That may be particularly problematic when you consider that directors, like many others, are becoming increasingly aware of the duties, responsibilities and potential liabilities which multiple directorships can bring – and are ever more reluctant to take on those directorships in the first place.

And who can blame them? If, as is often the case, a large and complex group of companies has evolved over a long period of time, lack of historical knowledge and a shortage of records may mean there are unknown issues which could give rise to future liabilities or reputational damage. Ask any finance director or risk manager whether they feel wholly comfortable with this so-called 'corporate memory loss' and it's a safe bet their response will be a resounding 'no'.

A well-structured, methodically-researched, project of corporate simplification can help to overcome all of these concerns. The objective of simplifying corporate structure should not be solely to reduce the number of companies per se, but also to reduce the risk attached to those companies retained. Bringing hitherto buried issues to the surface enables directors to deal with them in a planned and measured way. However bad an issue might be, discovering it and dealing with it internally is infinitely preferable to having it come as a bolt out of the blue as a result of some third-party claim.

Getting it right means collating as much information about each company and its history as possible. It means casting the net wide and consulting as many documents, and actively engaging with as many people, as you can think of (friendly ex-employees and pensioners can often be a great source of information). Yes, a company's assets and liabilities should be considered, but so too should be a full range of issues – whether it has (or had) employees, for example; whether it runs a pension scheme, or has any contractual obligations; whether it's involved in any ongoing litigation; or has outstanding insurance claims; or owns any intellectual property.

As well as using the findings of this group-wide review to make informed decisions about the retention or dissolution of companies within the group, a comprehensive record can be created of all the issues found, all the actions taken. Establishing this 'bible' can reduce the risk of future corporate memory loss and is a valuable by-product of the corporate simplification process.

Ideally, at the end of a successful corporate simplification project, not only should the number of subsidiaries have been reduced, but a new attitude will have been embedded within the group towards dissolution of inactive companies. Being proactive in dealing with companies when they come to the end of their useful lives is simply part of the responsibility of managing them from the cradle to the grave.

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