# If Your Company Goes Into Liquidation, Dividends Paid to Your Spouse May Be Investigated

Paying dividends to a spouse can look like sensible tax planning when a company is trading normally.

But if the company later goes into liquidation, those payments may be looked at very differently.

A liquidator will not simply see “family tax planning” and move on.

They may investigate whether the dividends were lawful, whether the company had sufficient profits to pay them, whether the spouse genuinely owned the shares, and whether the directors allowed money to leave the company when creditors should have been protected.

That is where a simple dividend arrangement can become a much bigger problem.

## Liquidation changes the lens

When a company enters liquidation, the liquidator’s role includes reviewing what happened before the liquidation.

That can include looking at payments made to directors, shareholders, spouses, family members and connected parties.

Dividends paid to a spouse may therefore come under scrutiny, especially where the company was already under financial pressure at the time.

The liquidator may ask:

1. Were the dividends properly declared?
2. Did the company have sufficient distributable profits?
3. Was the company solvent at the time?
4. Were creditors being paid on time?
5. Were there arrears with His Majesty’s Revenue and Customs?
6. Was the spouse a genuine shareholder?
7. Were the shares properly transferred?
8. Were the payments made into the spouse’s own bank account?
9. Did the spouse keep and control the money?
10. Was the arrangement genuine, or was it simply a way to move money out of the company?

These questions can quickly become uncomfortable if the paperwork is weak or the company was already struggling.

## Directors can be investigated

One of the points directors often do not realise is that liquidation can lead to an investigation into their conduct.

This does not mean every director has done something wrong.

But once a company enters liquidation, the liquidator may review the conduct of the directors and report concerns where appropriate.

That review may include looking at whether directors allowed dividends to be paid when the company could not afford them, whether company money was extracted improperly, and whether creditors were prejudiced.

If the Insolvency Service becomes involved, directors may also face questions about whether their conduct makes them unfit to be involved in the management of a company.

That is why dividends to spouses are not just a tax issue.

They can become part of a wider director conduct review.

## Dividends must be lawful

A company cannot pay dividends simply because there is cash in the bank.

This is a common mistake.

The company must usually have profits available for distribution. Cash in the bank does not automatically mean profit.

A company may have money in its account because it has not paid suppliers, tax, loans, rent or other creditors.

If dividends are paid without sufficient distributable profits, they may be unlawful.

In liquidation, a liquidator may seek repayment of unlawful dividends. That can affect the shareholder who received the money and potentially the directors who approved the payment.

This can be especially difficult where the dividends were paid months or years earlier and the money has already been spent.

## Payments to a spouse may attract closer scrutiny

There is nothing automatically wrong with a spouse owning shares or receiving dividends.

Many family companies are structured that way.

The problem arises where the arrangement does not reflect genuine ownership or where payments were made at a time when the company was in financial difficulty.

A liquidator may look at:

1. When the spouse became a shareholder.
2. Whether the share transfer was properly documented.
3. Whether Companies House records were updated.
4. Whether the company's statutory registers were updated.
5. Whether the spouse had voting rights.
6. Whether the spouse had rights to capital.
7. Whether the spouse had any real involvement or financial interest in the business.
8. Whether dividends were paid correctly according to the share rights.
9. Whether the company had the profits to support the dividends.
10. Whether creditors were left unpaid while family members received money.

The timing matters.

If shares were transferred years before any financial difficulty and dividends were properly paid out of available profits, that may be easier to explain.

If shares were transferred shortly before liquidation, or while the company had significant creditor pressure, the arrangement may be questioned more closely.

## The paperwork needs to tell the story

In liquidation, directors often have to explain decisions long after the event.

That is why paperwork matters.

A liquidator may ask for:

1. Board minutes.

2. Dividend vouchers.
3. Management accounts.
4. Year end accounts.
5. Profit and loss information.
6. Balance sheets.
7. Share transfer forms.
8. Company registers.
9. Bank statements.
10. Any accountant or tax advice relied upon.

If the paperwork is missing, vague or created after the event, the director may have a harder job defending the position.

The liquidator will usually follow the documents.

If the documents do not support the explanation, the director may be left trying to rely on memory.

That is rarely a comfortable place to be.

## Dividend waivers can create additional risk

Dividend waivers are sometimes used where one shareholder gives up their right to a dividend so that another shareholder receives more.

This may be acceptable in some circumstances, provided it is properly structured and supported by a genuine commercial reason.

However, in liquidation, dividend waivers can be looked at very carefully.

A liquidator may ask:

1. Why was the waiver used?
2. Was it signed before the dividend was declared?
3. Was it executed properly as a deed?
4. Was there a genuine commercial reason?
5. Did it artificially increase the payment to a spouse or connected person?
6. Could the company afford the dividend without prejudicing creditors?

If the waiver appears to have been used simply to move money to a spouse or family member while creditors were unpaid, it may create real difficulty.

## The director’s duties are central

Directors need to be particularly careful when the company is insolvent or approaching insolvency.

At that stage, creditor interests become increasingly important.

Paying dividends to shareholders, including a spouse, while creditors remain unpaid can raise serious questions.

A liquidator may consider whether the directors acted properly, whether they breached their duties, and whether the payments should be recovered.

Depending on the facts, the issues may include:

1. Unlawful dividends.
2. Misfeasance.
3. Breach of directors’ duties.
4. Preferences.

5. Transactions at an undervalue.
6. Transactions defrauding creditors.
7. Recovery claims against shareholders or connected parties.
8. Director disqualification concerns.

Not every case will involve all of these issues.

But directors should understand that once liquidation starts, historic payments can be reviewed through a much tougher lens.

## Warning signs directors should not ignore

Directors should take advice before paying dividends or changing share structures if:

1. The company has tax arrears.
2. Suppliers are being paid late.
3. The company is relying on creditor pressure to manage cash flow.
4. Loan repayments are being missed.
5. The company has received statutory demands or legal threats.
6. There are no reliable management accounts.
7. Dividends are being paid while the company is struggling.
8. A spouse or family member is receiving money but the records are unclear.
9. Share transfers have been made recently.
10. The company is already considering liquidation or insolvency advice.

These are the moments when directors need to pause.

Once the company enters liquidation, the opportunity to put matters right may already have passed.

## My practical view

Spouses can absolutely be shareholders.

Spouses can receive dividends.

Family company structures are not automatically wrong.

But if the company later goes into liquidation, directors need to be able to show that the arrangement was genuine, lawful and properly documented.

The key questions will be:

1. Was the spouse genuinely entitled to the dividend?
2. Was the dividend paid out of available profits?
3. Was the company solvent at the time?
4. Were creditors being paid?
5. Was the paperwork completed properly?
6. Was the director acting properly in the circumstances?
7. Was the arrangement defensible if investigated later?

If those questions cannot be answered clearly, the director may face serious difficulty.

## Final thought

Tax planning may look sensible when a company is healthy.

But if the company goes into liquidation, dividends paid to a spouse may become part of a wider investigation into the director’s conduct.

The question is no longer simply:

**“Was this tax efficient?”**

The question becomes:

**“Should this money have left the company at all?”**

That is why directors should not treat spousal dividends as a casual planning tool.

If the company is under pressure, get advice before making further payments, transferring shares or using dividend waivers.

Because once a liquidator is appointed, the paperwork, the timing and the reasoning behind every payment can come under scrutiny.

## Concerned about dividends paid before liquidation?

If your company is experiencing financial pressure, or you are concerned that dividends paid to you, your spouse or another shareholder may be questioned in a future liquidation, it is better to review the position early.

Book a confidential meeting with Vee Bharkhada to discuss the circumstances and understand the practical options available.

Book a meeting with Vee

## Important disclaimer

This article is provided for general educational and information purposes only. It is not legal, tax, accounting or insolvency advice and should not be relied upon as a substitute for advice based on your company’s particular circumstances.

The legal and practical consequences of dividends, share transfers and payments to connected parties will depend on the facts, the company’s financial position, the available records and the law applicable at the relevant time.

No director, shareholder or spouse should take or refrain from taking action solely on the basis of this article. Appropriate professional advice should be obtained from a suitably qualified legal, tax, accounting or insolvency adviser before making decisions or responding to any liquidator, creditor or regulatory investigation.