THE COMPANY TAX CHANGES AND HOW TO PLAN FOR THEM

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Carl Bayley BSc FCA

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By Carl Bayley BSc FCA

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About the Author

Carl Bayley is the author of a series of 'Plain English' tax guides designed specifically for the layman and the non-specialist. Carl's particular speciality is his ability to take the weird, complex and inexplicable world of taxation and set it out in the kind of clear, straightforward language taxpayers themselves can understand. As he often says himself, "My job is to translate 'tax' into English."

Carl enjoys his role as a tax author, as he explains, "Writing these guides gives me the opportunity to use the skills and knowledge learned over more than thirty years in the tax profession for the benefit of a wider audience. The most satisfying part of my success as an author is the chance to give the average person the same standard of advice as the 'big guys' at a price everyone can afford."

Carl takes the same approach when speaking on taxation, a role he frequently undertakes with great enthusiasm, including his highly acclaimed annual 'Budget Breakfast' for the Institute of Chartered Accountants.

In addition to being a recognised author and speaker, Carl has often spoken on taxation on radio and television, including the BBC's 'It's Your Money' programme and BBC Radio 2's Jeremy Vine Show.

Carl began his career as a Chartered Accountant in 1983 with one of the 'Big 4' accountancy firms. After qualifying as a double prize-winner, he immediately began specialising in taxation. He worked for several major international firms until beginning the new millennium by launching his own practice, through which he provided advice on a wide variety of taxation issues for twenty years, before deciding to focus exclusively on his favourite role as author and presenter.

Carl is a former Chairman of the Tax Faculty of the Institute of Chartered Accountants in England and Wales and a member of the Institute's governing Council. He is also a former President of ICAEW Scotland and member of the ICAEW Board. He has co-organised the annual Practical Tax Conference for the last eighteen years.

When he isn't working, Carl takes on the equally taxing challenges of hill walking and creative writing: his Munro tally is now 105 and he is currently waiting for someone to have the wisdom to publish his first novel, while he eagerly works on the next.

Carl lives in the Scottish Borders, where he enjoys spending time with his partner, Linda. He has three children and his first grandchild arrived in April 2021.

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Introduction

The March 2021 Budget included a huge raft of changes to the UK Corporation Tax regime, as well as confirming other changes already announced that are particularly relevant to companies. Some of the measures have immediate effect, some will come into force over the next few years, but all of them will have a major impact on company taxation in the UK.

The changes are so wide-ranging and fundamental that we at Taxcafe decided we should publish a new guide to help company owners, their accountants, and advisers, understand the impact of the changes on their companies, the tax planning opportunities available, and some of the pitfalls to be wary of.

In the long run, many companies will inevitably see increases in their Corporation Tax bills. But we will explore a range of options to mitigate the impact of those increases. We will also see that, in the short term, there are many opportunities to make additional Corporation Tax savings, both in terms of cashflow, and long-term absolute savings.

While some of the Corporation Tax changes do not affect all companies, taken as a package, the changes are relevant to every company: large, medium-sized, or small; profitable or loss-making; whether carrying on a trade, investing in and letting property, or some of both.

While we will, of course, primarily focus on the costs and benefits of the tax changes, we will never lose sight of the bigger picture where tax savings must be weighed against the commercial impact of the company's actions.

In Chapter 1, we will begin by looking at some of the background to the Corporation Tax increases coming into force in April 2023 (although they will affect some companies as early as May 2022), as well as providing a brief summary of how Corporation Tax works to help you get the most out of the rest of the guide.

Chapter 2 deals with the Corporation Tax increases and looks at many of the extra complexities involved, including transitional rules for accounting periods spanning the changes on 1st April 2023 and the definition, and impact of, associated companies. We will see that having an additional associated company will sometimes have a tax cost, but could also sometimes save tax; or it may make no difference at all. We look at what the costs and benefits are, how to avoid those costs, and whether, commercially, the action needed to save tax is justified.

Chapter 3 looks at marginal rate tax planning. Generally speaking, this is all about timing. With many companies' Corporation Tax rates set to increase over the next few years, the timing of deductible expenditure, taxable income, and capital gains on property disposals, can make a big difference to the company's tax bill. Of course, the timing of a lot of income and expenditure cannot be altered, or it would not make commercial sense to do so, but there are also many items that are worth considering and we cover the main ones in this chapter.

In Chapter 4 we look at the extraordinary opportunity presented by the 130% 'super-deduction' announced in the Budget: where companies can deduct up to 130% of their expenditure on items like new trucks and vans, machinery, furniture, and computer equipment, from their taxable profits. However, while the super-deduction presents excellent tax-saving opportunities for some companies, there are also many instances where it will be better for the company to wait until a later accounting period when they may enjoy even greater tax savings on their expenditure. The commercial reality of some of the super-deduction's limitations is also examined with a crucial focus on after tax cost rather than how much tax is saved.

Chapter 4 also covers other important changes to tax relief for companies on its asset purchases, including expenditure on fixtures and fittings, and cars (both electric and conventional); as well as other items not qualifying for the super-deduction. We look at how all the changes fit in with the existing capital allowances regime and how companies can get the best tax relief for their capital expenditure under any circumstances. In particular, we look at some rather unexpected pitfalls awaiting many companies spending even relatively modest amounts in early 2022.

In Chapter 5, we look at the temporary extension to the rules that allow companies to carry trading losses back to earlier accounting periods to obtain Corporation Tax relief. This extension could allow some large companies to claim additional tax refunds of up to £760,000. Smaller companies will benefit too, with a speedier, ‘stand alone’ claim process that could quickly bring in extra tax refunds of up to £76,000.

Quick refunds will be invaluable to many companies still struggling under the impact of the coronavirus crisis, but for those that expect to ‘bounce back’ there are some tricky choices to be made. We look at the options available and the factors to be considered.

Finally, in Chapter 6, we examine the issue of ‘salary versus dividends’ and look at what the Corporation Tax changes mean for company owners wishing to extract funds from their company as tax efficiently as possible. This complex subject never seems to get any simpler, but we consider all the issues to be addressed and look at most of the likely combinations you will encounter. Despite the topic’s complexity, we also summarise our findings as simply as possible.

You will find many opportunities to mitigate the impact of the forthcoming Corporation Tax increases, and to make additional savings in the meantime, detailed in this guide.

While it was inevitable we would face tax increases, and we all need to do our part to help with the country’s (indeed the world’s) economic recovery, company owners have every right to protect themselves, their business, their company, and their family. Saving tax through sensible planning measures is part of that: and that’s exactly what this guide will help you to do.

Chapter 1

Background to the Tax Changes

1.1 WHY THE CORPORATION TAX RATE IS GOING UP

The coronavirus crisis has had an enormous financial cost. Government spending since March 2020 has leaped to unprecedented levels. Much of this has been vital to support the UK economy, and to save lives.

But we all know there will be a price to pay at some stage and the Government has decided to begin this process by targeting companies. Why?

The cynic in me says this is because companies don't have a vote. But there are other factors at play. Some of the after tax profits made by the larger companies operating in the UK eventually flow overseas in the form of dividends: a loss to the UK economy.

Our current, low, rate of Corporation Tax (19%) is attractive and highly competitive internationally. But every country in the world will be facing its own financial crisis so company tax rates are likely to increase elsewhere too. So, perhaps our Government is gambling that we can increase our Corporation Tax rates and yet still remain competitive. This idea is perhaps supported by the fact President Biden has called for a minimum global corporate tax rate for the largest multinational companies of 21% (coincidentally, the same as the current US corporate tax rate).

The Government may be thinking that targeting companies instead of individuals will not reduce the amount of money flowing through the UK economy. But, aside from the obvious fact that company owners will have less after tax profits to pay themselves from, lower after tax profits in companies also mean less money left to invest, less money left to pay suppliers, less many left to pay employees, and higher prices charged to customers to compensate. They may not hit us in the pocket as directly and as obviously as an Income Tax increase, but the Corporation Tax increases will affect us all.

Such a large hike in Corporation Tax rates seems rather out of character for a Conservative Government. Indeed, previous Conservative Chancellors have pointed to the fact that economic studies suggest lower Corporation Tax rates will actually produce greater tax yields in the long run (as they stimulate investment and attract business into the UK).

But these are exceptional times calling for exceptional measures. Government forecasts suggest the Corporation Tax increases will raise around £16 to £17 Billion per year. Unfortunately, given that the Government projects additional borrowings of almost £600 Billion to fund its coronavirus crisis support package, this is just a drop in the ocean: there will need to be a lot more tax rises to make any serious impact on the national debt. But I guess we won't see those until after the next General Election. After all, our multi-trillion pound debt is only going to reach 97.1% of GDP before then.

But these 'telephone number' size figures are for the politicians to worry about. On a national level, I hope the Government's gamble pays off. For ourselves, we just have to plan for the changes as they affect our own companies: and that's what this guide is all about.

1.2 INTRODUCTION TO CORPORATION TAX

All of a company's profits, income and capital gains for an accounting period are added together and treated as a single total sum of 'profits chargeable to Corporation Tax'. You will occasionally see this important phrase appear in later sections, although I will more often simply refer to a company's 'profit' for an accounting period. In either case, I mean the company's total taxable income, profits, and capital gains for that period.

With the exception of dividend income, the same tax is paid on all types of income or gains received by the company, and at the same rate. However, as we shall see in the following chapters, the rate of Corporation Tax paid by the company is dependent on a number of factors, including the date its accounting period begins and ends and the total level of its profits and gains from all sources.

Companies are generally exempt from Corporation Tax on dividend income received; although dividends received in accounting periods ending after 31st March 2023 may create an additional tax cost in some cases.

Financial Years

Corporation Tax operates by reference to 'Financial Years'. Just to make life even more confusing than it already undoubtedly is, the Financial Year is slightly different to the tax year ending on 5th April that applies to income received by individuals.

A Financial Year is the year ending on 31st March in any calendar year, but is officially described by reference to the calendar year in which it began. Hence, for example, the 2021 Financial Year is the year commencing 1st April 2021 and ending 31st March 2022. It is important to be aware of this official terminology, as this is what is used on the Corporation Tax Return.

Periods Spanning Two Financial Years

Where your company's accounting period does not end on 31st March, it will generally span two Financial Years. The profits of the accounting period are then split across the two Financial Years on a pro rata basis. For example, a profit of £100,000 for a twelve month accounting period ending 31st December 2021 would be split as follows:

2020 Financial Year: £100,000 x 90/365 £24,658
2021 Financial Year: £100,000 x 275/365 £75,342

Where the Corporation Tax rate is the same in both Financial Years, this split is completely academic. However, where the Corporation Tax rate changes from one Financial Year to the next (as it will in 2023), the split can have a real impact: as we shall see in the next chapter.

Leaping Ahead

To take another example, a profit of £100,000 for a twelve month accounting period ending 31st December 2024 would be split as follows:

2023 Financial Year: £100,000 x 91/366 £24,863
2024 Financial Year: £100,000 x 275/366 £75,137

As we can see, the fact that 2024 is a leap year makes a slight difference to this calculation. Furthermore, it is worth pointing out that the 2023 Financial Year ending on 31st March 2024 will be a 'Leap Financial Year' of 366 days' duration. This will lead to a few minor, but curious, quirks in some company's Corporation Tax calculations, as we shall see later in the guide.

Corporation Tax Payments

For companies with annual profits not exceeding £1.5m, Corporation Tax is currently payable nine months and one day after the end of the accounting period. For example, the Corporation Tax for the year ending 31st March 2022 is due by 1st January 2023.

Larger companies must pay Corporation Tax in quarterly instalments and the Government is currently consulting on the possibility of extending this regime to smaller companies some time after the next General Election.

The £1.5m threshold for quarterly instalments must be divided among any associated companies in a similar way to the lower and upper limits for the small profits rate (see Section 2.4).

1.3 CLOSE COMPANIES

The vast majority of private companies are 'close companies' and this concept is important for a number of tax purposes.

Broadly speaking, a company is a 'close company' if it is under the control of five people or less. This generally arises when any group of five or less individuals, together with other individuals deemed to be 'connected' with them (see Appendix C), own more than 50% of the company's share capital (although control can sometimes arise in other ways). A company where all the shareholders are directors is also a close company.