Taxlab
CHARTERED CERTIFIED ACCOUNTANTS

Corporation tax

If your business is a company, you need to submit corporation tax returns and pay corporation tax on your profits.

Although you are likely to use accountants to prepare your returns and calculate your tax liability, you cannot afford to ignore corporation tax until the year end. The way you finance and manage your business can have a significant impact on the final bill.

1. Calculating taxable profits

Tax is levied on all the profits made during an accounting period.

Profits can arise from several sources

- Trading profits: income from your company's trading activities, less allowable expenses such as labour and raw material costs etc.
- Capital gains: the profits made from selling certain company assets. For example, if you make a profit from selling a factory, it will be taxable unless you reinvest the money. Note: capital gains on the sale of shares in a trading subsidiary may be exempt.
- Income from letting out land or buildings.
- Interest on any money held on deposit. Unlike individuals, companies generally receive interest without tax having been deducted.
- Most other forms of income or capital gain. For example, share of partnership income; any profits made on currency movements.
- Profits from different sources have to be calculated separately, because different rules apply to income and expenditure on each.
- The rules are complex. Ask your accountant, tax adviser or auditor for advice.

Tax allowances and expenses

Taxable profits can be reduced by deducting various corporation tax reliefs and allowances, for example:

- For business assets such as plant and machinery, capital allowances are deducted from taxable profits rather than depreciation.
- Most business expenses are tax allowable but there are exceptions such as entertaining expenses.

Companies are taxed on the profits made in an accounting period

- The accounting period normally runs to their financial year.
- The end of an accounting period can also be triggered by the company going into liquidation or ceasing to trade.

- Tax rates are set for the tax year, which (for corporation tax purposes) runs from 1 April to 31 March.
- Where the company's accounting period and the tax year do not coincide, the profits must be time-apportioned to decide which rate should apply.

Tax on overseas activities depends on where the company is resident for tax purposes

- Companies resident in the UK pay corporation tax on their worldwide profits.
- Companies resident elsewhere normally pay corporation tax only on their profits from a UK branch or agency. Non-UK profits are generally taxed (often at higher rates) elsewhere.
- Check your situation with your accountant or tax adviser.

2. How much tax?

From April 2017 the single rate of corporation tax is 19% on all profits, reducing to 17% by 2020.

- Businesses with profits that can be attributed to patented inventions and certain other intellectual property can elect to pay a reduced rate of 10% tax on those profits. See ‘Minimising the tax bill’.
- For the financial years April 2015 to 6 April 2017, there was a single rate of corporation tax set at 20% on all profits.

Prior to 6 April 2015 there were three corporation tax bands, depending on your profit.

- If your profits were between £300,000 and £1.5m, you were eligible for marginal relief.

3. Payment

Companies are responsible for assessing their own liability to corporation tax and for ensuring that all the money which is due is paid on time.

Most companies have to pay within nine months and one day of the end of their accounting period

- This rule applies to small and medium-sized companies (ie those with profits of up to £1.5m).
- Tax must be paid in full at the due date, whether or not HMRC is challenging the figures shown on the return.
- Interest is charged on late payments.

Larger companies have to pay the tax due in quarterly instalments

- The first instalment has to be paid six months and 14 days after the end of the preceding accounting period (ie halfway through the accounting period to which the payments relate).
- Two further quarterly payments then have to be made with the balance payable within three months and 14 days of the end of the accounting period.
- Companies with profits in excess of £20m will be required to pay their corporation tax bill in instalments on the third, sixth, ninth and 12th month after the end of their accounting period from April 2017.
- Special rules apply where the accounting period is not 12 months.

All companies have to submit their corporation tax return online

- The corporation tax return must be made within 12 months of the end of the period of account. There are penalties for failing to file on time.
- If HMRC disputes any of the figures in the corporation tax return, the company may face an enquiry or a demand for extra tax. The inspector normally has 12 months from the date the return was filed make enquiries.
- Company tax returns, corporation tax and related penalties and interest must be submitted and paid electronically.

HMRC assumes that you will employ a qualified accountant or tax adviser

- Your accountant or adviser can deal with correspondence and help you with corporation tax.
- HMRC will send you the appropriate forms as soon as your company is registered with Companies House.
- Your local tax office can assist with minor problems.

Personal tax accounts with HMRC

- All small businesses and personal tax payers now have their own tax account (as from April 2016).
- The accounts will allow people to see their tax transactions across the range of business taxes including self-assessment, corporation tax, VAT and PAYE for employers and to make payments at any time.

The company bank account

Owner managers should avoid using the company bank account as a second personal account.

Every payment must be accounted for.

- If cash payments to owner managers cannot be identified as salary or dividends, they will be treated as loans from the company.
- Such loans can have serious tax consequences. To avoid these, it is generally necessary to repay the loan within nine months of the year end.
- Use of the company's bank account for personal expenditure also creates extra work for the company's accountants, and may lead to increased fees.

4. Losses

Losses can sometimes be used to reduce the corporation tax bill. However, their use is subject to strict rules, to prevent tax evasion.

Trading losses can be offset against other profits made in the same accounting period

- Trading losses can also be carried back against profits made in the preceding accounting period. To do this you must make a separate claim to HMRC when you submit your corporation tax return.
- Alternatively, they can be carried forward and set off against future profits from the same trade. This is registered automatically when you submit your tax return so you don’t need to submit a separate claim.

- They cannot be carried forward if the company changes hands and there is a major change in the business. So there is no point in buying or selling companies purely for the sake of their tax losses.
- From April 2017, the amount of profit that can be offset by losses carried forward is limited to 50% for profits above £5m.

Other companies within the same group may be able to make use of a company's trading losses

- To qualify, at least 75% of the shares must be owned by the parent company.
- There are other restrictions. For example, when a company joins or leaves the group.

Capital losses can only be offset against capital gains

- They cannot be offset against trading income.
- However, they can be carried forward indefinitely, so they should always be recorded, even if they cannot be used immediately.

5. Minimising the tax bill

Increasing profits is generally more important than avoiding tax. However, you may be able to reduce unnecessary tax payments.

Consider using loans, rather than shares, to finance the company

- Interest on loans is an allowable expense against profits, whereas dividends on shares are not.

Ask your professional advisers about methods of reducing profits

- These need to reduce taxable profits without damaging the company or its prospects.
- Take advantage of capital allowances and the Annual Investment Allowance available on equipment purchases. The AIA limit currently stands at £200,000 but will increase to £1m on 1 January 2019.
- If possible, reinvest the proceeds of any asset sale and use 'rollover relief' to reduce capital gains.

Consider using benefits in kind as a way to take money out of the company

- Employers have to pay national insurance (NI) on almost all benefits in kind. But employees do not pay NI on most benefits.
- Income tax has to be paid on such benefits, but they qualify as earnings when you calculate how much you can pay into a personal pension scheme.
- The company must purchase the benefit (eg medical insurance), rather than reimbursing you.

Consider using dividends, rather than a higher salary

- The Dividend Tax Allowance is £2,000 per year from April 2018. Tax on dividend income in excess of £2,000 will be taxed at 7.5% for basic rate tax payers, 32.5% for higher rate tax payers and 38.1% for additional rate payers. This is a significant reduction in benefit from the previous allowance of £5,000.
- You may need advice on dividend payments. You may have to pay some salary to working shareholders to compensate them for the disproportionate dividends paid to (say) retired shareholders.

- Payment by dividend may limit your rights to state benefits and the amount you can contribute to an approved pension scheme, as the amounts do not count as earnings. However, they will count for the purposes of calculating whether you are liable for basic or higher rate tax.

Your tax planning options may be more limited for a personal service company

- If you work under the control and management of any of your clients, you may be caught by the IR35 rules and be deemed to receive a salary larger than the one you actually draw.
- If you run such a company, seek professional help.

Consider whether any of your profits can be attributed to intellectual property (IP)

- Under the Patent Box scheme you can elect to pay a reduced 10% rate of tax on profits associated to your IP.
- The profits must come from patent rights you sell or license, sales of patented products or products containing a patented invention, intellectual property infringement income or damages or compensation relating to your patent rights.
- To claim the reduced rate, you must make an election in your tax return within two years of the end of the accounting period to which the profits relate.

R&D tax relief

Consider whether you can make a claim for research and development (R&D) tax relief.

HMRC provide tax relief of 230% on qualifying R&D expenditure for small or medium-sized enterprises

This can:

- reduce the corporation tax payable
- provide a tax credit
- increase tax losses which can be carried forward to offset against future taxable profits.

Large companies can claim R&D tax relief of 130% on qualifying R&D expenditure

- Large companies can claim an 'above the line' pre-tax credit of 12% for 2018/19 (11% 2017/18). The tax credit is mandatory from 1 April 2016.
- Companies do not have to be developing or creating leading edge technology to claim R&D relief.
- There are no spending limits.
- Losses can be carried forwards or backwards.

Signpost

- Find an ACCA accountancy firm for accounting and tax advice.
- Find a solicitor for advice on the legal aspects of corporation tax through the Law Society.
- Find corporation tax guidance on GOV.UK.
- Make a corporation tax enquiry to HMRC (0300 200 3410).

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