

corporate tax

It may be some years before a start-up company begins to make a profit, but unfortunately that does not mean it can ignore tax issues. Even if tax is not an issue on day one of the new business, it is important that the entrepreneur understands the company's future obligations and establishes the company to minimise future tax liabilities. The main UK taxes payable by companies are corporation tax, value added tax, income tax and national insurance contributions.

Corporation tax

A company is liable to UK corporation tax on all its profits and chargeable gains, whether made in the UK or elsewhere.

1 Rates of tax

1.1 Large companies: The main rate of corporation tax payable by all companies with annual taxable profits above £1,500,000 is 23 per cent for the financial year running from 1 April 2013 to 31 March 2014. This rate of the tax also applies to small companies which are "close investment holding companies".

1.2 Small companies: Small trading companies will pay tax for the year commencing 1 April 2013 at the following rates:

Profit band	Tax rate
£0 - £300,000	20%
£300,001 - £1.5m	23.75%

However, if two or more companies are associated by reason of common control, the thresholds at which the small companies' rates cease to apply and the ordinary 23 per cent rate of corporation tax begins to apply, are reduced correspondingly for each company.

The ordinary rate of corporation tax is set to fall to 21 per cent from 1 April 2014 and 20% from 1 April 2015..

Taxable profits and deductions

In computing the company's taxable profits on its trading activities, certain deductions from receipts and accrued income are permitted.

- o Revenue expenditure incurred by the company "wholly and exclusively for the purposes of the trade" (although certain items, such as business entertaining, are specifically disallowable).
- o Capital expenditure incurred by the company on certain assets (eg, industrial buildings or plant and machinery) acquired for the purposes of the company's trade may give rise to "capital allowances". Such allowances, when available, are normally allocated over several years. The rates at which such allowances are available depend on the precise nature of the asset. An annual investment allowance treats capital

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- o expenditure on plant and machinery as deductible in full (up to £250,000 pa in the two years commencing 1 January 2013 but falling to £25,000 pa from 1 January 2015).
- o A small or medium sized enterprise which incurs qualifying R&D expenditure in excess of £10,000 annually may be entitled to tax relief equivalent to 225 per cent of the expenditure incurred. This relief can be set against current profits or carried forward against future profits. Alternatively, in the case of a company which is operating at a loss in a financial period, the tax relief may be given up in return for claiming a tax credit payable in cash and worth a proportion of the tax relief available.
- o Interest costs can normally be deducted from the company's total profits.
- o A statutory deduction may be available in respect of shares provided to employees or directors who pay less than market value to buy those shares.

Special rules apply to expenditure incurred while a company is preparing to trade but has not yet begun its trading activities and tax relief for such expenditure, while often available, should not be assumed.

2 Chargeable gains

Corporation tax on chargeable gains may be payable on the disposal of a capital asset if the consideration received (or treated as received) for the disposal exceeds the acquisition cost and any other deductible expenses or reliefs available. In some circumstances, trading companies can defer tax on chargeable gains by way of "roll-over" relief on the replacement of assets used in the business.

3 Losses

Trading losses can be offset against other profits, including capital gains, made in the same accounting period as the trading loss. Thereafter, losses may be carried back against profits of the previous year. Any surplus losses not used up by carry-back, may be carried forward and used against profits arising from the same trade in future accounting periods.

4 Close company rules

If the company is controlled by five or fewer persons, then it will be classified as a "close company". "Close company" status can have tax implications in a number of situations. In particular, if the company lends money or advances credit to any individual shareholder, option holder, loan creditor or any "associate" of such a person, a charge to tax is incurred at the rate of 25 per cent of the amount of the loan or advance. If and when the loan or advance is repaid, this tax can be reclaimed from the HM Revenue & Customs.

5 Transfer pricing

Transactions between associated persons on non-arm's length terms, which would give either party a tax benefit, may be subject to "transfer pricing" rules. These rules are typically an issue where one person is in the UK and one outside the UK. If so, the transactions are taxed as though arm's length terms had been agreed. Interest payments, management charges and import/export prices on nonarm's length terms can be counteracted under these provisions. In many cases small and medium sized enterprises are exempt from the transfer pricing rules.

6 Payment and procedures

For small companies corporation tax is not due until nine months after the end of each accounting period. Under the Corporation Tax Self-Assessment rules the company is under an obligation to file a tax return to the HM Revenue & Customs 12 months after the end of each accounting period in which all of the company's tax liabilities are disclosed to HM Revenue & Customs and penalties can be imposed for failure to do so. The company will require qualified staff and, in all probability, advice from external accountants to discharge these compliance obligations.

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Value added tax (VAT)

7 VAT registration

A company making taxable supplies of goods and/or services for which the value exceeds (in the tax year 2013-2014) £79,000 per annum, must register for VAT with HM Revenue & Customs. The company will be under a duty to account for VAT (output tax) on all its taxable supplies. Certain supplies are, however, exempt from VAT (eg, supplies of land, such as renting out premises, unless an option to tax has been made). VAT is added to the cost of the supply charged to the customer to whom the supply is made.

8 Payments and returns

The company must pay on to HM Revenue & Customs any VAT due at the end of each accounting period (usually quarterly but monthly in certain cases). The VAT due is VAT on its taxable supplies less some or all of the VAT the company pays on supplies made to the company (input tax). Input tax is recoverable if it relates to taxable supplies the company makes or intends to make. Where a business makes exempt supplies, this may restrict the amount of input tax which the trader is permitted to recover or set-off against his output tax. For low turnover businesses, VAT compliance can be undertaken through the annual accounting scheme (taxable turnover less than £1,350,000) or a flat-rate scheme (taxable turnover less than £150,000).

Special rules apply to cross-border transactions, whether involving goods or services, and the rules differ depending on whether a transaction is an intra-EC transaction or involves one or more non-EC persons.

PAYE and national insurance

9 Employees – income tax

Income and benefits from employment or from serving as a director of a company are charged to UK income tax as employment income under the tax code. Income tax is charged on benefits in kind from employment or serving as a director (including many forms of share-based incentives) as well as monetary payments.

10 PAYE

10.1 What is it?

The Pay-As-You-Earn (PAYE) method of deducting income tax from salaries and wages applies to all income from employment and directorships. PAYE does not generally apply to benefits in kind but there are exceptions to this rule. It is the employing company's duty to deduct income tax from the pay of its employees/directors. If an employer fails to do so, the employer will be required to pay to the HM Revenue & Customs the tax which he should have deducted and, in addition, penalties may be imposed.

10.2 Compliance

The employer must complete tax returns in respect of income and benefits provided to employees and supply these to the HM Revenue & Customs in respect of each tax year within strict statutory time limits. In addition, the employer must provide information to employees about their taxable income to enable employees to complete a tax return under the self-assessment rules.

10.3 Share incentives

Particular care should be taken if shares or options are made available to employees. In some cases, such shares or options can give rise to PAYE liabilities. A company needs to consider whether employee shareholdings can be structured so that only capital gains tax applies and not income tax. If this is impossible, a company must ensure it has a suitable indemnity from the employee shareholder/optionholder to cover any PAYE liabilities and, to the extent appropriate, NICs.

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National insurance contributions (NICs)

An employer is required to account for NICs on his employees' behalf to the HM Revenue & Customs, and the employer must pay additional employers' contributions. Contributions are earnings-related, although above an upper earnings threshold, employee's contributions apply at only 2 per cent.

Employer's NICs will be a liability of the company and, normally, it is unlawful to attempt to pass this cost on to employees. However, special arrangements can be made to transfer the cost of employer's NICs to employees in relation to share options and, in some cases, employee held shares. In normal circumstances, employer's NICs will represent an expense of the company which is deductible for corporation tax purposes. Employer's NICs can be a tax cost associated with the provision of share-based incentives to employees if, on the facts, NICs are found to apply.

Some steps to take

- o Register for VAT.
- o Set up your payroll systems.
- o Find a good accountant to help with corporation tax returns.
- o Ensure that tax planning is part of your overall business planning.

This section of LaunchPAD has been prepared on the basis of this law on 10 January 2014.

Contact

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