# Introduction

The approach of a company's year end is an important time to look at opportunities to save tax. A number of tax-saving actions have to be taken by that date, otherwise the opportunity could be lost forever. Changes in legislation could also remove some options. The last few months of a company's year are also a good time to consider company planning generally, and tax is often an important part of this. Companies should nevertheless review their taxation position regularly, especially if they are making quarterly payments of corporation tax.

The points covered in this topic are not intended to be a substitute for professional advice, and in some cases it might be best to take no action. Whatever the company's circumstances, its tax planning should not be left until the last minute.

# Income and expenditure

The general tax planning strategy should normally be to defer income and make full use of all available allowances and deductions. The announcement in the Budget on 23 March 2011 to reduce the main rate of corporation tax from 28% to 26% on 1 April 2011, and then reduce that main rate by 1% each year to 23% will increase the value of this strategy. The small profits rate of corporation tax also be reduced to 20% on 1 April 2011.

Deferral of income and acceleration of expenses is particularly important if the company's profits are between £300,000 and £1.5 million, as profits in these bands are taxed at the relatively high marginal rate of 27.50% in the financial year beginning 1 April 2011. As this is higher than the corporation tax main rate of 26% on profits above £1.5 million, there may be an advantage in deferring profits to a period in which they will not be taxed at the marginal rate.

## Income

Income can be deferred in several ways:

- Ensuring that goods or services are sold in a later accounting period.
- Selling goods on consignment or on sale or return, so that the income need not be recognised until the goods are actually sold.
- Investing surplus funds in investments that give rise to deferred income (outside the loan relationships regime) or capital gains.
- If a company has a seasonal business, the company's accounting period could perhaps be extended or shortened to maximise the availability of tax relief for loss-making periods. Care must be taken to comply with company law, because there are restrictions on how often a company can change its accounting period, and in any case it cannot be longer than 18 months.
- In some cases, a company could consider changing its accounting policies for specialised trading activities, for example, builders with long-term contracts. The current policies might not be the most appropriate way of reporting income for tax purposes. In certain situations, a change in policy can defer income to later periods. However, the accounting policies must be applied on a consistent basis from one year to the next, and this could restrict such tax planning measures.

## Expenditure

There are several ways in which a company can maximise deductions for expenses in an accounting period. Planned expenditure, for example on repairs, could be brought forward or, in some instances, a provision could be made in the accounts for future costs where these costs

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can be clearly quantified. In general, tax relief is allowed for provisions made in accordance with generally accepted UK accounting practice. The following items merit particular review.

### Bad debts

The debtors' ledger should be reviewed in detail so that provisions and/or impairments can be made for bad debts. Relief for such debts now falls within the company loan relationship rules. HMRC will only allow the write-off of debt for tax purposes where specific debts have been identified: a time-based provision across all debts will not be accepted.

### Stock

The company can make a specific provision against slow-moving, damaged or obsolete stock, but a general provision is not allowed against tax.

The company might be able to change the way it values stock, but great care needs to be taken.

### Closure/redundancy

To obtain a tax deduction for redundancy costs not yet incurred, redundancy notices should be issued before the end of the accounting period.

### Bonuses

It might be possible to bring forward remuneration intended for the following year, thus advancing tax relief.

- Bonuses to directors and staff could be paid before the year end, but the PAYE and national insurance implications for the company and the individuals concerned must be considered.
- Alternatively, bonuses could be accrued, but they must then be paid within nine months of the end of the period, otherwise they will be deductible for tax purposes only in the accounting period in which they are paid.

### Pension contributions

If the company has a registered occupational pension scheme, tax relief is given for contributions actually paid in the year, rather than the amounts provided for in the accounts.

- Tax relief is given if the contributions are paid wholly and exclusively for the purposes of the business. HM Revenue & Customs (HMRC) may object to tax relief for large pension contributions for an employee who is related to a controlling director. Objections to contributions on behalf of controlling directors are rare. Another instance where HMRC might disallow a deduction for pension contributions is if they are paid as part of arrangements for the company to stop trading.
- The deduction for pension contributions may have to be spread over up to four years where there is an increase over 210% in the level of employer's contributions from one period to the next, and that increase is £500,000 or more.
- In a family-controlled company, the pension scheme should be reviewed to see whether the benefit levels can be enhanced without causing tax problems.
- If the company has no pension scheme, it should consider establishing a suitable scheme, which can offer valuable tax advantages.
- Aggregate contributions by the employer and employee should not normally exceed the annual allowance (£50,000 in 2011/12 subject to carried forward allowances).

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- Each member's tax-exempt pension fund, or its equivalent value in benefits, should not exceed the lifetime allowance (£1.8 million in 2011/12, subject to transitional reliefs).

- A company can also contribute to employees' and directors' personal pension schemes. Care is needed to ensure that the total contributions from employer, employee and value added to other final salary pension schemes the individual may be a member of, do not exceed the individual's annual allowance. Inputs to pension schemes above the annual allowance may be subject to a tax charge at the taxpayer's marginal rate.

### Investment in a new trade

A company that plans to embark upon a new trade might generate tax losses in its early years, especially if it incurs capital expenditure eligible for capital allowances.

- The new trade should ideally be started before the end of the current accounting period, because this will accelerate tax relief for any losses.

- If possible, the new trade should be established within an existing trading company so that any losses can be set against that company's profits. It can be transferred to a new company at a later date, if desirable.

### Donations to charity

A company's donations to charity are tax deductible.

- The company does not have to deduct tax from the donation or make any gift aid declaration.

- There are no limits on the size of donations.

- There are strict limits on any benefits the company can receive in return for the donation.

- Tax relief for donations made in the accounting period is given against the company's profits but cannot create or enhance a loss.

### Research and development

Companies should review the amount of their expenditure on research and development (R&D). Small and medium-sized companies (SMEs) are given tax relief on 200% (for expenditure from 1 April 2011) of the actual costs. The company must currently spend at least £10,000 per year on qualifying revenue expenditure, but this minimum threshold is due to be removed in 2012. For large companies, tax relief is on only 130% of the qualifying costs.

- R&D means activities treated as such under normal UK company accounting practice. The expenditure must be incurred on staffing costs, consumable stores, certain other costs such as power, fuel, water and software, or sub-contracted work. It must be related to a trade carried on by the company or be expenditure from which it is intended that such a trade will be derived.

- A company is small or medium-sized for this purpose if it, together with any other company in which it holds more than 25% of the capital or voting rights, has fewer than 500 employees and at least one of the following conditions is met:

    - Annual turnover is not more than €100 million (approximately £84 million).

    - Net assets are not more than €86 million (£72 million).

- Relief is capped at €7.5 million for each R&D project.

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- The annual expenditure limit is reduced for accounting periods of less than one year.
- If the expenditure gives rise to an unrelieved trading loss, the company can claim payment of a tax credit instead of carrying the loss forward, but this tax credit is currently limited by the amount of PAYE and NICs paid for the accounting period. This limit on the tax credit is due to be removed in 2012.

# Capital expenditure

A company should review its capital expenditure programme and, if necessary, bring forward expenditure that qualifies for capital allowances, so that it is incurred in the current accounting period.

## 100% allowances

Companies can get 100% tax relief in the year of purchase on the first £100,000 (£25,000, from 1 April 2012) a year of expenditure on most types of equipment by claiming the annual investment allowance (AIA). Any balance of expenditure above this threshold attracts writing down allowances (WDA) at a maximum of 20% a year, or 10% for certain assets.

- The AIA is proportionately increased or reduced for accounting periods that are longer or shorter than 12 months.
- Companies that form a group are entitled to only one AIA between them.
- Where companies do not form a group but are controlled by the same person or persons, they will share the AIA if they are 'related', which means sharing business premises or having similar activities.
- Companies that spend more than the AIA can choose the expenditure on which they claim the AIA. To maximise future WDAs, the AIA should be claimed first on expenditure that only attracts the 10% WDA.

A 100% allowance is available for capital expenditure on R&D, designated energy-saving equipment, qualifying water-efficient technologies, qualifying conversions or renovations of flats above commercial property.

A 100% allowance is available to a company of any size on the cost of buying a low emission car.

- The car must be first registered after 16 April 2002 and bought new.
- The car must either emit not more than 110g/km of carbon dioxide ($CO_2$), or be electrically propelled.
- A 100% allowance is available on new zero-emission goods vehicles from 1 April 2010 until 31 March 2015.

A 100% business premises renovation allowance is available to individuals and companies that incur capital expenditure on bringing qualifying business premises in disadvantaged areas back into business use. This allowance will now be available until 11 April 2017.

- The allowance is given in the period in which qualifying expenditure is incurred.

## Writing down allowances

Capital expenditure that does not qualify for the AIA or other 100% allowances, and any balance of expenditure brought forward from previous years, is pooled and qualifies for an annual WDA.

- The main rate of WDA is 20% on general plant and machinery and motor cars with $CO_2$ emissions of 160g/km or less bought after 31 March 2009.
- Expenditure on motor cars with $CO_2$ emissions of more than 160g/km bought after 31 March 2009, long-life assets, integral features of a building (e.g. electrical and heating

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systems) and thermal insulation is pooled separately in a special rate pool and qualifies for WDA at 10%. Long-life assets are those with a life of at least 25 years, if annual expenditure on such assets exceeds £100,000.

- WDA on motor cars bought before 1 April 2009 for more than £12,000 is restricted to £3,000, but such cars will be transferred to the main pool or special rate pool from April 2014.
- The main rate of WDA will reduce to 18% on 1 April 2012 and the special rate will reduce to 8% on the same date.

## Timing

Careful timing of purchases and disposals of assets can advance an allowance or defer a charge.

- It may be worth bringing forward or delaying expenditure to avoid exceeding the AIA limit in any one accounting period.
- Disposals of pooled assets with high sale proceeds should be delayed until the next accounting period, because the disposal will reduce the pool of expenditure available for capital allowances.
- A company approaching the £100,000 limit of expenditure on long-life assets might consider deferring further expenditure on long-life assets, to remain entitled to 20% allowances. Cars and certain other assets are excluded from the definition of long-life assets.

## Buildings

A detailed review of expenditure on buildings should be undertaken to ensure that all expenditure allowable for tax is identified.

- Expenditure could be allowable as revenue costs or might be eligible for capital allowances as plant, at 100%, 20% or 10%.
- The company should ensure that any invoices from building contractors are analysed carefully to maximise the availability of tax deductions.
- Tax relief for repairs to ‘integral features’ of a building may be restricted. If in any 12-month period the cost of repairing an integral feature is more than 50% of the cost of replacing it, the expenditure must be treated as capital expenditure to be subject to the AIA or the special rate WDA, currently at 10%. Careful timing of such expenditure should avoid the restriction.

## De-pooling of short life assets

Plant and machinery (excluding cars) can be ‘de-pooled’ for capital allowances when it is judged to have a ‘short’ useful life for the business of less than eight years from the end of the accounting period in which it was bought (four years for assets purchased before 1 April 2011). If the expenditure does not qualify for the 100% AIA, an election can be made to de-pool it. In this case the WDA is calculated for the asset individually and the allowances are accelerated if the asset is indeed disposed of within the expected short life period.

## Intangible assets

Companies are entitled to tax relief for purchases of intellectual property, goodwill and other intangible assets. The relief is based on the amortisation shown in the accounts, but companies can opt for relief at 4% a year instead. Disposals and revaluations of intangible assets will generally give rise to a tax liability, but rollover relief is available where the sale proceeds are reinvested in other intangible assets. Intangible assets that were in existence on 1 April 2002

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(when the present tax regime started) generally continue to be taxed under the capital gains rules, but rollover relief is available under the new rules.

The rules for intangibles should be taken into account in any planning involving expenditure on or disposals of intangible assets. In particular, where rollover relief may be available, companies should make sure they acquire qualifying new assets within a period starting one year before and three years after the disposal.

## Trading losses

Where the company is likely to incur tax losses in the current accounting period, the planning measures outlined above can be used to increase the amount of the tax losses available for relief.

- In general, trading losses can be carried back to the immediately preceding year. As a result, a tax repayment is likely to arise.
- A temporary extension to this relief allows companies to carry back losses for up to three years, with later years' profits relieved first.
- Only losses for company accounting periods ending between 24 November 2008 and 23 November 2010 can be carried back more than one year.
- The amount of losses that can be carried back to the immediately preceding year is unlimited. After carry-back to the immediately preceding year, a maximum of £50,000 of any unused losses is then available for carry-back to the earlier two years.
- Losses arising in the last 12 months before a trade ends can also be carried back (without limit) for up to three years. The availability of profits in earlier periods could influence the choice of date for a cessation.

## Corporation tax payments

Companies that pay the main rate of corporation tax (currently 26%) have to make quarterly payments of corporation tax, normally on the 14th day of the 7th, 10th, 13th and 16th months after the beginning of the accounting period. The payments are based on the company's estimated corporation tax liability for that period.

- A company pays the main rate of corporation tax if its taxable profits are at least £1.5 million, and are thus counted as 'large' for this purpose. This profits threshold is divided equally between a company and its associated companies and is reduced for accounting periods shorter than 12 months.
- Interest is charged where any tax payable in instalments is paid late.
- Instalment payments for an accounting period are not required from companies that were not 'large' in the previous accounting period, provided expected current year profits are not more than £10 million.
- A company is not treated as large if its corporation tax liability does not exceed £10,000.
- The payments must include any liability under the transfer pricing rules (which generally apply only to large companies), charges arising under the controlled foreign companies legislation and tax payable on any loans to shareholders.

Companies at risk of having to pay tax by instalments might be able to use the planning measures outlined above to reduce their taxable profits to below the threshold, thereby helping their cash flow.

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# Capital gains

A company's capital gains are calculated under the chargeable gains rules as they apply to companies, but they are then included in the company's total profits chargeable to corporation tax.

- Capital losses not set against gains in the current year can only be carried forward and offset against future gains.
- Trading losses can be offset against capital gains of the same year or the previous 12 months.

Companies cannot claim entrepreneurs' relief. However, unlike individuals, companies get an indexation allowance, under which base acquisition values are revalued in line with movements in the retail prices index (RPI) over the period of ownership.

The different rates of tax on chargeable gains for individuals and companies, and the availability of entrepreneurs' relief and indexation allowance, should be taken into account in any decision about whether an asset should be held within or outside a company.

## Capital losses

A company that has realised capital gains might be able to sell investments to realise a capital loss to offset against the gains. Alternatively, gains could be realised where a company has made capital losses.

Unlike individuals, companies are not subject to specific share identification rules designed to prevent the 'bed and breakfasting' of shares and securities – selling them and buying them back shortly afterwards to realise gains or losses but not change the underlying investments.

However, a company undertaking such an exercise could fall foul of the capital losses targeted anti-avoidance rules (TAARs) introduced with effect from 5 December 2005. These disallow losses arising from 'any arrangement... the main purpose, or one of the main purposes, of [which] is to secure a tax advantage.'

## Trading losses and capital gains

If a company is likely to have trading losses that it cannot carry back against earlier profits, it could sell investments to realise capital gains. These gains can then be offset against the trading losses. This is especially important if the company intends to stop trading, as trading losses cannot be carried beyond the cessation of trade.

## Negligible value claims

A company might own investments that have become virtually worthless. If so, a negligible value claim can be made, thereby creating a capital loss. A company has two years from the end of the accounting period in which the loss arose to make the claim and treat the loss as arising in the earlier period.

A company with a 31 March 2010 year end therefore has until 31 March 2012 to claim this relief for investments that became of negligible value in that accounting period. HMRC keeps a list of listed shares that it regards as coming into this category. It is also possible to claim relief for the loss of goodwill bought before 1 April 2002 as part of a business that has subsequently failed.

## Timing of asset sales

If a company is planning a sale of an asset with a large potential gain, it might be worth delaying the sale until the start of the next accounting period. This would give the company an extra 12 months before it will have to pay tax on the gain.

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Some companies' profits fluctuate and could be taxable at the marginal rate of tax (currently 27.50%) in some periods. It might be possible to time the disposal so that the gain arises in an accounting period for which the company is liable to tax at only the small profits rate (20% from 1 April 2011).

### Rollover relief

Tax on the disposal of land and buildings, and of fixed plant and machinery, can be deferred. To secure full rollover relief, all the sale proceeds must be reinvested in new qualifying assets in the period starting 12 months before and ending three years after the date of the disposal. Partial relief is also available. If the company has made gains that can be rolled over in this way, a company's capital expenditure plans should be reviewed to ensure that suitable qualifying assets are acquired within these time limits.

### Substantial shareholdings

Companies are exempt from tax on certain disposals of shares.

- The company selling the shares must be a trading company or member of a trading group.
- For this purpose, a group is defined as for CGT but with a 51% ownership test rather than 75%.
- The seller must have owned at least 10% of the company in which shares are being sold for a period of 12 months within the 24 months before the sale.
- The company in which the shares are being sold must have been a trading company or holding company of a trading group since the beginning of the 12-month period of 10% ownership mentioned above.
- Both the seller company and the company whose shares are being sold must retain their trading status immediately after the sale.

Companies planning to sell shares at a profit might be able to time the sale or otherwise arrange the transaction in order to ensure they satisfy the conditions for this exemption.

If a company is considering selling part of its trade, it may be able to save tax by hiving down that part into a new subsidiary which can be sold free of tax after 12 months. However, there are many other issues to take into account.

## Groups of companies

Several additional year end tax planning possibilities exist where companies form a tax group. The general aims should be to ensure that:

- Corporation tax is not paid while losses are available within the group.
- Losses are relieved as early as possible at the highest rate.
- Losses are not carried forward in companies where profits are unlikely to arise.
- Profits chargeable at the marginal rate of 27.50% are minimised.

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## Tax rates

The structure of corporation tax rates has the effect of penalising companies with profits in the marginal band. For the year ending 31 March 2012:

- Companies with profits up to £300,000 pay 20% on their profits.
- Companies with profits between £300,000 and £1.5 million are taxed at the small companies' rate of 20% on the first £300,000 and at a marginal rate of 27.50% on the excess.
- Companies with profits of £1.5 million or more pay tax at 26% on all their profits.

Where two or more companies are under common control, these limits are divided equally between them.

From 2011 until 2015, the rates will be progressively reduced. The small profits rate will be maintained at 20% and the main rate will fall from 28% to 23%. In consequence:

| Year end | 31 March 2012 | 31 March 2013 | 31 March 2014 | 31 March 2015 |
|---|---|---|---|---|
| Std rate | 26% | 25% | 24% | 23% |
| Marginal | 27.5% | 26.25% | 25% | 23.75% |

Groups should therefore minimise the number of active companies and control the incidence of profits among the companies in order to maximise use of the small profits rate and minimise taxation at the marginal rate.

This could be achieved by:

- Selective routing of profitable contracts.
- Careful use of commercially justifiable management charges.
- Trading between companies.
- Suitable group relief claims.

Groups whose profits are mostly taxable at the main rate might be able to ensure that profits of smaller companies within the group are taxable only at the small profits rate.

## Group structure

The group structure should be examined to ensure that maximum advantage is taken of the various grouping provisions.

## 75% group

Within a 75% group, the following tax advantages are available:

- Offset of current year trading losses against the profits of other group companies.
- Transfer of assets without a capital gain or loss arising, and without any liability to stamp duty.
- An election can be made to enable capital losses to be set against another company's gains.
- Transfer of a trade without tax disadvantages, so that, for example, capital allowances already given are not lost and losses carried forward are preserved.

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- A group of companies is regarded as one company for rollover relief purposes under the chargeable gains and intangible assets rules.
- Relief is available from stamp duty land tax (SDLT) for a range of land transactions within a group and for certain reorganisations. There are, however, clawback provisions if certain events occur within three years of the intra-group transfer.

### 51% group

A 51% group has the following tax advantages:

- Large companies can make their quarterly instalment payments of corporation tax on a group-wide basis without specifying the individual companies' tax liabilities. This helps reduce their exposure to interest on tax paid late. Group companies wishing to do this must make advance application to HMRC. Not all companies in a 51% group have to be included in the arrangement.
- A group VAT registration can reduce the administrative burden of VAT and eliminates the need to charge VAT on transactions between the companies (group VAT registration is also available to companies controlled by one individual or a business partnership).
- Substantial shareholding exemption is available for the disposal of qualifying investments in trading companies meeting the conditions prescribed.

### Splitting into divisions

As an alternative to a group structure, an existing group could consolidate its activities into divisions within one company.

The potential advantages of such action are:

- Reduced administrative and tax compliance costs.
- Less likelihood of penalties under self-assessment, as fewer returns and payments have to be made.
- All capital gains and losses are automatically grouped.
- No need for management charges.
- Unrealised profits are not taxed.
- There are no associated companies. The use of the small profits rate is therefore not restricted. But equally, groups paying tax at the main rate cannot exploit the small profits rate by selective routing of profits into smaller group companies.

A reorganisation of the group structure can normally be achieved at no tax cost, but the potential legal and accountancy costs of the exercise should be compared with the likely benefits.

### Elections

Some of the above tax advantages are only available if the necessary election has been made between the various companies. If there are changes to the companies within the group structure, any elections must be reviewed so that all new group members are included.

## Shareholder-controlled and family companies

Some additional tax planning is possible in a company with a small number of shareholders.

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## Corporation tax rates

The marginal and main rates of corporation tax can be avoided more easily in a family or shareholder-controlled company by the following planning strategies:

- Paying salary and bonuses rather than dividends (although this will involve a national insurance cost – see below).
- Minimising the number of associated companies (companies under common control but which do not necessarily form a group). The profit limits that determine corporation tax rates are divided equally between associated companies.
- Equalising profits of associated companies, where total profits are not more than the small profits limit of £300,000. Where profits are higher, a non-equal spread between companies might produce the optimum result.
- Paying pension contributions into a UK registered pension scheme.

## Dividends versus salary/bonus

A family company should review whether it is preferable to pay dividends or salary/bonus. Many factors must be considered, and detailed calculations might be necessary before a decision can be reached.

- Paying dividends is normally more attractive than paying salary or bonuses because national insurance contributions (NICs) are not payable on dividends.
- There are some disadvantages to the payment of dividends rather than salary or bonuses, for example:
  - ➢ It could restrict an employee's tax-relieved personal contributions to a pension, as they cannot exceed the amount of the individual's earnings. However, employers' contributions could be paid instead, as they are not restricted by reference to salary.
  - ➢ Individuals with dividend income rather than earnings can find difficulties in raising residential mortgage finance or claiming income benefits under permanent health (income protection) policies.
  - ➢ The 10% tax credit on dividends cannot be repaid. Shareholders who do not have sufficient other income will waste their personal allowance. Where shares are held by family members in this position, the company could pay them a salary up to the level of their unused personal allowance, as well as dividends, if they carry out some work in the business.
  - ➢ It could increase the value of the shares for the purposes of inheritance tax (IHT) and CGT. The impact of IHT will normally be limited because business property relief at the rate of 100% is given on transfers of shares in qualifying unlisted companies that do not hold non-business investments. Similarly, entrepreneurs' relief will usually reduce the size of the potential CGT bill.

## Retaining profits in the company

Shareholders should consider whether surplus funds should be paid out to shareholders and directors or retained within the company. This is particularly relevant where the shareholders expect to sell the company at a profit (or enter into a members' voluntary liquidation) at some stage in the future.

- Entrepreneurs' relief reduces the effective tax rate to 10% on capital gains up to a lifetime limit of £10 million (£5 million before 6 April 2011). This makes a disposal of shares more attractive than receiving dividends or bonuses.
- However, shares qualify for entrepreneurs' relief only if the company is a trading company. In order to qualify as a trading company, non-trading activities, assets and income must not

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be substantial. Substantial is broadly interpreted as 20%. A large holding of surplus funds could jeopardise the company's trading status.

### Personal service companies

Companies affected by the special rules for personal service companies (IR35) should consider whether to pay additional salary or bonuses in order to avoid income tax and NICs on a deemed salary payment on 5 April. The timing of any additional remuneration will depend on the company's accounting date relative to 5 April. A change of accounting date might also be beneficial.

### Directors' current accounts

Where a close company (a company controlled by five or fewer shareholders or controlled by its directors) makes loans to its participators – broadly, shareholders and their associates – the company must pay tax equal to one-quarter of the amount of the loan, unless the loan has been repaid within nine months of the end of the accounting period.

- The overdrawn account can be cleared in several ways, without necessarily having to repay it in cash. For example, the company could declare a bonus or dividend up to the amount of the loan, although the income tax and NIC implications must be considered.
- Deficits on directors' current accounts can occur because the directors have had cash advances to meet business expenses for which they have not yet submitted a claim for reimbursement. They should do so before the end of the accounting period, because the expenses will also then be deductible in the company accounts.
- If a director's current account cannot be cleared by any of these methods, the tax due on the loan must be included in the company's self-assessment and paid with the corporation tax.

Where tax has been paid on a loan in a past period, the tax is repaid nine months after the end of the accounting period in which the loan is repaid. The best time for participators to repay past loans is therefore towards the end of an accounting period, because this minimises the delay before the company receives the tax repayment.

HMRC may object where participators repay loans at the end of an accounting period and withdraw the money again at the start of the following period. Loans to directors of more than £5,000 may also make the director liable for income tax on a benefit in kind for the period for which the loan was outstanding.

## Close investment companies

A close investment company is a special type of company that must pay the main rate of corporation tax on all its taxable income. It is worth trying to ensure that companies do not inadvertently become close investment companies. This can be achieved by introducing into the company a suitable income stream or trade well before the end of its accounting period.

## Claims and elections

An essential part of a company's year end tax planning procedures is to review the time limits for tax claims and elections. If the time limits are missed, the company might have to pay additional tax unnecessarily. The time limits vary but the most important are those that must be made within two years of the end of a company's accounting period.

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They include:

- Set-off of losses against the current or preceding accounting periods.
- Claim for enhanced tax relief for R&D revenue expenditure.
- Surrender of, and claims for, group or consortium losses. Claims must be made in a tax return.
- De-pooling of short-life assets for capital allowances.
- Capital allowances claims, which must be made in a tax return.
- Elections for notional transfers of assets between group companies to enable capital losses to be set against another company's gains.

A company that makes up its accounts to 31 March must make these claims for the year to 31 March 2010 by 31 March 2012.

# Value added tax

VAT can be complicated and the penalties for getting it wrong are quite severe. A company's VAT affairs must be kept under close review, and the approach of the company's year end is an ideal time for that review.

- A company that is not registered for VAT should review its level of turnover every month. It should register for VAT on time once the turnover for the preceding 12 months exceeds the threshold – currently £73,000.
- Where a company makes both taxable and exempt supplies, it should review its method of calculating recoverable VAT, and review the tests for partial exemption to see if it falls within the de minimis limits. The rules allow a variety of methods and a different one might reduce the amount of irrecoverable VAT.
- A company should review the supplies it has made to ensure that VAT has been accounted for correctly. Supplies made to companies in the same group often cause problems. For UK companies within a 51% group, a group VAT registration removes the need to charge VAT on inter-company supplies. It might also help reduce the amount of irrecoverable input tax.
- If the company makes overseas supplies or purchases of services from other countries where the reverse charge may apply, either within the EU or outside it, the VAT treatment of the supplies should be examined very carefully. VAT on expenses incurred in other EU countries may be reclaimable.
- A company should review its debtors and claim VAT relief on any debts that it has written off. Bad debt relief can be claimed from six months after the date when payment was due.
- There is a four-year time limit (increased from three years with effect from 1 April 2009) for recovery of VAT overpaid in the past. The limit also applies to bad debt relief and recovery of VAT paid on goods bought before the company registered for VAT. Companies should review past periods to ensure that any claims for VAT recovery are made in time.
- A company with an annual turnover of £1.35 million or less could consider opting to account for VAT on the basis of cash received and cash paid. Companies that use 'cash accounting' need to watch their turnover figures carefully. Using cash accounting also gives immediate relief for any subsequent bad debts.

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- A company can also opt to submit VAT returns once a year rather than quarterly, provided its annual turnover is not more than £1.35 million. Although the scheme requires monthly payments, it will ease the administrative burden of operating VAT.

- The flat rate scheme for small businesses is available where turnover is less than £150,000.

# Employee costs

## Company cars and other benefits

The tax effects of benefit packages for employees must be reviewed regularly. The following points are among those that should be considered:

- The taxable benefit on the provision of a company car is a percentage of the car's list price, which is graduated according to the level of the car's $CO_2$ emissions. The company car is no longer as tax-efficient as it once was for many employees, especially those with larger cars; however, it can be tax-efficient for some employees, e.g. those with small, low emission cars (120g/km or less) and high private mileage.

    - ➢ Employees could be offered a cash alternative to a company car and claim tax-free reimbursement for business mileage in their own cars. This would eliminate the administration costs of providing company cars.

    - ➢ The company could opt for lower emission or cheaper cars.

- Employers that provide free fuel for company cars should keep their policy under review, as this is now a very highly taxed benefit. It may be beneficial to switch to paying tax-free mileage allowances for business mileage instead.

- An employer can make a loan to an employee of up to £5,000 without any tax implications. Interest-free loans could help employees buy their own cars.

## Employee share ownership schemes

Share and share option schemes can be a useful means of rewarding employees while also providing them with a medium- to long-term incentive. Companies should consider the timing of any share issues or acquisitions by employees in conjunction with their year end tax planning.

- The share incentive plan (SIP) allows employers to give employees up to £3,000 of shares a year free of tax and NICs. Employees can also buy up to £1,500 of shares a year out of pre-tax salary, and employers can match these shares with up to two free shares for each share bought. The value of the free shares and the costs of setting up and running the scheme are tax deductible. Companies get a corporation tax deduction when they pay into a SIP trust, rather than when the shares are awarded to employees, subject to certain conditions.

- Smaller higher-risk companies can grant enterprise management incentive (EMI) share options of up to £120,000 per employee, subject to an overall company limit of £3 million. These share options offer considerable tax benefits to the employee. The employer's costs are tax deductible.

- In order to encourage employee share acquisition under both HMRC approved and unapproved schemes, companies can claim a corporation tax deduction for the market value of the shares when the employee acquires them, less any amount the employee pays for the shares.

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# Tax planning key points

In any tax planning exercise it is important to be clear about priorities. Saving tax is important, but it needs to be kept in proportion. There are many other factors to consider, such as:

- Although the company might save tax by using a particular strategy, it should leave enough money to meet its business needs.
- It is not enough for an investment to be tax-efficient: it should be a good investment in itself, without necessarily taking the tax advantages into account.
- Flexibility is almost always desirable, even if it involves additional costs or saves less tax. Circumstances could change, and it might become necessary to unravel arrangements.
- The costs and general inconvenience that could be involved in implementing some strategies might outweigh the potential tax savings.
- As far as possible, company tax planning should be kept reasonably simple and straightforward. It makes it much easier to keep the main objectives in sight and to explain the plans to anyone else who might be involved.
- A reduction in the company's taxable profits is usually mirrored in the company's profit and loss account and balance sheet.
- A company that is trying to increase its borrowings or aim for a listing on the stock market or Alternative Investment Market (AIM) might prefer to demonstrate stronger results rather than save tax.

*This guide is for general information only and is not intended to be advice to any specific person. You are recommended to seek competent professional advice before taking or refraining from taking action on the basis of the contents of this publication. The guide represents our understanding of the law and HM Revenue & Customs practice as at September 2011, which are subject to change.*

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