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CORPORATION TAX – PLANNING TIPS

Corporation Tax has certainly been making the headlines recently, with Boris Johnson announcing that, if re-elected, the planned 2% cut in the Corporation Tax rate would not now go ahead in April 2020, which is anticipated to save the Treasury £6bn in 2020/21.

Around two million trading companies in the UK will be familiar with paying Corporation Tax at the current rate of 19% on any company profits. Directors of those companies also know how that percentage can eat into those profits when the time comes to extract them.

Last year alone, Corporation Tax netted the Treasury £55.1 billion. While the 2018/19 figure represented a 2% rise on the previous year, it also increased for the sixth successive year. With that in mind, what can you do to ensure you minimise your Corporation Tax bill and keep more of your company's hard-earned profits?

Choosing The Right Business Structure

According to Companies House, 672,980 companies were incorporated in 2018/19 – an increase of 8.5% on the previous year and the highest number of annual incorporations since the depth of the recession in 2009/10. More than a third of companies were aged between one and four years, with many making the move from sole trader or partnership. The current 19% rate of Corporation Tax can make incorporating more appealing than paying the current marginal rates of income tax for higher earners.

However, as set out in more detail in my article earlier this year, consideration must also be given to the marginal rates of income tax which will be charged on the extraction of any profits from your limited company.

Utilise Tax Reliefs

Corporation Tax bills can be reduced through tax planning and identifying reliefs to which your company might be entitled. Research and development (R&D) relief is available for both smaller and larger companies that work in innovative projects within science or technology. Small and medium sized companies are able to subtract 130% of their qualifying costs from their annual profits on top of a basic 100% deduction (230% in total).

Companies that generate and hold income from a patent can reduce their Corporation Tax bill from 19% to 10% on a specific element of their profits by electing into the patent box scheme.

Capital Allowances and the Annual Investment Allowance

You may be able to offset 100% of certain capital costs, such as any equipment, machinery or commercial vehicles, you buy for use in your company. These costs extend to demolition expenses for your plant and machinery, and integral features, such as air conditioning, lighting, heating systems and hot and cold water systems.

The Annual Investment Allowance (AIA) lets you deduct the full cost – up to £1 million per annum until 31 December 2020 – of such items from your profits before you work out your Corporation Tax liability.

The timing of such capital expenditure which might qualify for the AIA is important. If, for example, you have a 31 December year end and are planning on purchasing a new piece of machinery or equipment etc. in the near future, you would be well advised to complete the purchase on or before 31 December 2019 in order to claim the AIA in your tax computations for the current accounting period. This should then reduce your Corporation Tax bill which will be payable by 1 September 2020. If you delay the purchase until the new year, you will not generally see the benefit in the reduction to your Corporation Tax bill until 1 September 2021 – a few days can make a significant difference!

Extracting Profits

As discussed previously, there are various methods by which you can extract profits from your limited company. They can include:

- Salaries;
- Dividends;
- Pension contributions;
- Interest on any money that directors/shareholders may have lent to the company;
- Rent for any properties owned by directors/shareholders and used by the company;

Each of these has different tax implications for the directors/shareholders and the company, so it is important to consider them individually, depending on your specific circumstances.

It is worth bearing in mind when considering all of the options above that retaining profits in companies (if practicable and desirable) which are currently subject to a tax rate of 19%, rather than extracting all of the profits, can still be attractive.

As mentioned above, each individual's circumstances will be different and specific advice is therefore essential. If you wish to discuss your tax affairs and those of your company we would be pleased to hear from you. The above is for general guidance only and no action should be taken without obtaining specific advice. May we take this opportunity to wish you all an enjoyable festive season.

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