viewpoint tax news

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Welcome to the September monthly tax newsletter. These newsletters are designed to keep you informed of the latest tax issues.

We hope you enjoy reading the newsletter; remember, we are here to help you so please contact us if you need further information on any of the topics covered.

LIQUIDATING A COMPANY - IS IT A CAPITAL GAIN?

One of the anti-avoidance measures being introduced by the latest Finance Bill potentially changes the way that certain payments to shareholders will be taxed. This may result in payments following some company liquidations being taxed as dividends instead of capital gains.

The Government is concerned that the new higher rates of income tax that have applied to dividends since 6 April 2016 may tempt some shareholder / directors to extract value built up within their companies in a capital form, rather than paying out the retained profits as dividends. This is because capital gains are generally taxed at a lower rate than income, possibly as low as 10% where entrepreneurs relief is available.

For example, a higher rate taxpaying shareholder receiving £100,000 on the liquidation of his company would pay £32,500 (32.5%) if the anti-avoidance applies, whereas CGT would be just £10,000 (10%) if entrepreneurs relief is available. Consequently, new stricter rules are being introduced to apply to transactions on or after 6 April 2016.

WHEN IS A LIQUIDATION TAXED AS INCOME?

For the new anti-avoidance rules to apply, the company being wound up must firstly be a close company and the individual must have held at least a 5% interest in the company (ordinary share capital and voting rights).

A further condition is that the individual (or connected person) continues to carry on the same or a similar trade or activity to that carried on by the wound-up company within the two years following the distribution.

It must also be reasonable to assume, having regard to all of the circumstances that the arrangements appear to have a tax advantage as one of the main purposes.

CAN WE OBTAIN CLEARANCE PRIOR TO THE LIQUIDATION?

Accountants and tax advisors requested that the new anti-avoidance rules should provide a formal clearance procedure prior to the transaction, thus providing certainty as to whether or not the payment would be taxed as income or capital. Unfortunately, there is no formal clearance procedure. HMRC have however received a number of clearance requests from taxpayers and have confirmed that it is not their general practice to offer clearances on recently introduced legislation with a purpose test.

HMRC have therefore drafted a standard reply that sets out a small number of examples and they are working on more detailed guidance, which should be published before the end of this year.

This is a very complex area and we suggest that you contact us before you consider liquidating your company.

POSSIBLE NEW LOOK-THROUGH ENTITY?

In the March Budget it was announced that the Government are considering the introduction of a completely new system of small company taxation and have asked the Office of Tax Simplification (OTS) to consider this possible new system in more detail.

It is proposed that the new system, if introduced, would apply to micro-entities with 9 or fewer employees and would tax shareholders directly on their company profits in proportion to their shareholdings as if the company was a partnership or LLP. For example, if Mr and Mrs Bloggs each owned 50% of the share capital of Bloggs Trading Ltd, and the company made a profit of £120,000, there would be no corporation tax to pay but they would each be taxed on their £60,000 share whether or not that amount was distributed to them.

It is felt that this would level the playing field between the taxation treatment of a small limited company and an unincorporated business. The Government and OTS are also considering the introduction of protected asset status for unincorporated businesses to align the owners' liability with that of limited company shareholders.

Both proposals may have significant tax and commercial implications for your business and we will keep you posted of further developments.

VAT ON INCORPORATION OF A BUSINESS

Despite the new dividend rules and the possible introduction of a new "look-though" entity many unincorporated businesses are still considering trading as a limited company. It is also important to consider the VAT implications of incorporation.

Where the new company carries on the same kind of business as the predecessor, the transfer of the trade and assets will normally be regarded as a transfer of a going concern (TOGC) and no VAT will be charged on the transaction. Further conditions are that there is no significant break in trading and the company must be VAT registered from its first day of trading.

Particular care is required where properties are transferred on incorporation where these are within the capital goods scheme or the option to tax has been exercised. We can of course assist you to make sure all tax implications are considered.

SHOULD WE KEEP THE SAME VAT NUMBER?

It is possible for the new company to keep the same VAT number as the predecessor business when it registers for VAT. However, we would normally advise that the new company should apply for a new VAT registration number as retention of the old VAT number means that the new company takes over the potential VAT liabilities of the business, including penalties for VAT errors in the previous four years.

BUYING A LOSS MAKING COMPANY

Another important announcement in the March Budget was the proposed relaxation in the rules for setting off a company's losses against the profits of future periods. These proposed changes that will allow set off against profits of any source are currently being consulted on and, if enacted, will apply to losses arising from 1 April 2017 onwards. Until then the set off of losses remains restricted, particularly when there is a change in the ownership of the company.

Currently, where there is both a change in the ownership of a company and also a major change in the nature or conduct of the trade carried on by that company within a 3 year period, the carry forward of trading losses is denied from the date of the change ownership. This measure is clearly designed to restrict the utilization of losses following a company sale.

HMRC take a great deal of interest in the way in which the trade is carried on during the run up to the sale and also post sale and have recently reissued detailed guidance as to how they interpret the rules based on previously decided cases.

For example, changes to improve company efficiency and rationalizing the product range are not viewed as major changes. However, changing the customer base or market sector being supplied may be seen as a major change, thereby blocking the carry forward of trading losses against future profits.

This can be a significant factor in business sales and we can advise you accordingly.

MERGER OF TRADES FOLLOWING AN ACQUISITION

HMRC have recently won a case before the Upper Tier Tribunal that the trading losses of a competitor company could not be set off against the profits of the acquiring company following the merger of the trades of the two companies. The two companies in question were both involved in the retail trade where 4 loss making department stores were merged with 3 profitable stores. The court held that the trading losses should be streamed and could only be set against future profits of the 4 loss making stores, overturning a previous decision by the First Tier Tribunal.

BUYING THE TRADE AND ASSETS OF THE TARGET COMPANY

Note that if instead of buying the loss-making company, the trade and assets are acquired, then the trading losses will lapse and will not be available to the purchasing company. This however may be commercially more attractive as the purchaser will not take over the liabilities of the vendor company.

Other important tax considerations would be the transfer of plant and machinery, including fixtures, at market value rather than tax written down value, and the ability to obtain corporation tax relief for the value of intangibles, but not goodwill.

Remember to get in touch with us if you need support in connection with buying or selling a business.

NOTIFICATION OF CHARGEABILITY

As set out in this month's tax diary, individuals are required to notify HMRC by 5 October 2016 if they are not within Self-Assessment and receive income or gains on which tax is due.

Many employees without significant other income do not receive a Self- Assessment Tax return as their tax is collected under PAYE. For example, if they start renting out a property or make a capital gain they may be required to notify chargeability.

The six-month time limit ensures that the taxpayer can be sent a tax return in sufficient time to complete it within the normal return cycle for the year.

Failure to meet the deadline means the taxpayer is liable to a financial penalty.

The maximum penalty is the net amount of tax due, but unpaid, at 31 January following the tax year in which the liability arises. This means that even if notification is made after the six-month time limit, the penalty can be eliminated if the taxpayer pays the full amount of the tax due on or before 31st January.

TAX DIARY OF MAIN EVENTS

DATE	WHAT'S DUE
1st September	Corporation tax for year to 30/11/15
19th September	PAYE & NIC deductions, and CIS return and tax, for month to 05/09/16 *(due 22 September if you pay electronically)*
1st October	Corporation tax for year to 31/12/15
5th October	Deadline for notifying HMRC of chargeability for 2015/16 if not within Self-Assessment and receive income or gains on which tax is due
19th October	PAYE & NIC deductions, and CIS return and tax, for month to 05/10/16 *(due 22 October if you pay electronically)*

FURTHER INFORMATION OR ADVICE

If you would like further information or advice about any of the issues raised in this newsletter or any other tax-related matter then Steve Bird would be delighted to hear from you.

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