

Finance Bill - Other corporation tax changes

(Lecture B1199 – 21.08 minutes)

Rate of corporation tax

As expected, corporation tax will remain at 19% from April 2020 and this rate will apply for FY2020 and FY2021 (Clause 5 and 6).

The current legislated rate is 17% (from s.46 Finance Act 2016). When preparing financial statements under FRS 102 or IFRS, deferred tax on timing differences reversing in accounting periods straddling 1 April 2020, or starting from that date, should be calculated at 17%.

This is because both FRS 102 and IFRS require that tax is calculated at rates enacted, or substantively enacted, by the balance sheet date. Finance Bill 2020 is unlikely to be substantively enacted before the end of March (or even April).

Example

A company has a year ended 31 December 2019. It has taxable timing differences of £120,000 of which £40,000 are expected to reverse in the year ended 31 December 2020 and the remainder after this.

Its deferred tax liability at 31 December 2019 should be calculated as:

	£
Reversing in 2020: $(19\% \times 91/366 + 17\% \times 275/366) 17.497\% \times £40,000$	6,999
Reversing after 2020: $17\% \times £80,000$	<u>13,600</u>
	<u>20,500</u>

The fact that the rate is set to remain at 19% should be disclosed in the notes to the financial statements if it would materially change the deferred tax balance or the tax expense in the profit and loss account.

Quarterly instalment payments (Lecture B1199 – 21.08 minutes)

Normal corporation tax is due 9 months and one day after the end of the accounting period but there is an accelerated quarterly instalment payment regime for large companies and now very large companies.

A large company is one with taxable profits over £1.5m and liability of more than £10,000 with thresholds proportionately reduced if there are related 51% group companies and if the accounting period is less than 12 months.

A very large company is one whose profits exceed £20m per year, again as long as the tax liability is more than £10,000 and with the limits also reduced as above.

HMRC have identified that there are companies not normally chargeable to tax but become so because they have chargeable gains accruing. Often, they will become

chargeable to corporation tax on the day of the gain and then immediately cease to be within charge, so having a one-day accounting period. These companies would fall within the very large company regime if their profit exceeds £54,795 and have a corporation tax liability of more than £27.40.

Falling within the very large company regime would mean that they would have to pay all their liability on the day of the disposal.

Clause 25 of the Finance Bill amends the relevant regulations so that these companies will be treated as large companies and so the corporation tax will be due 3 months and 14 days after the end of the accounting period. The legislation has effect for accounting periods beginning on or after 11 March 2020.

R&D expenditure credit

This relief mainly impacts on large companies but can also apply to certain costs incurred by small companies that are not eligible for SME enhancement. The RDEC is, as the name suggests, a credit which arises to eligible companies who are undertaking a qualifying activity.

Companies with no corporation tax liability may be able to reclaim the credit as a cash payment or use it to reduce other liabilities.

The tax credit is increased from 12% to 13% for expenditure incurred from 1 April 2020 (Clause 27).

Also announced at the Budget in relation to R&D costs were:

- there will be a consultation on widening the scope of the RDEC to include data and cloud computing costs as qualifying R&D expenditure
- the planned introduction of the cap on the payable tax credit in the SME R&D schemes will be delayed until 1 April 2021. This would see repayable tax credits capped at 3 x the PAYE liability for the accounting period. The Government wants more time to think about circumstances where the cap would not apply.

Corporate Intangible Fixed Assets

Intangible fixed assets created before 1 April 2002 have traditionally been treated as capital assets for corporation tax purposes unless purchased from an unrelated party after that date.

For assets falling within the intangible fixed assets (IFA) regime, the tax treatment more closely follows the accounting treatment so that there are more opportunities to get tax relief on the costs associated with such assets. In particular there is the chance to get tax relief for the ongoing amortisation or impairment of such assets.

Clause 30 introduces legislation to include relief for pre-1 April 2002 intangibles and to change the provisions for fungible assets.

Pre-FA 2002 intangibles

The current s882 CTA 2009 applies the IFA rules to assets falling within one of the following three categories:

1. Created by the company on or after 1 April 2002
2. Acquired by the company on or after that date from an unrelated party
3. Acquired by the company on or after that date from a related party but only where condition A, B or C is met
 - A is that where the vendor is a company, the asset was within the IFA regime before acquisition
 - B is that related party had acquired it after 1 April 2002 from an unrelated party
 - C is that it was created by the related party on or after 1 April 2002

The new legislation will state that assets will fall within the IFA rules if one or more of the following conditions is met:

1. The asset is created by the company on or after 1 April 2002
2. The asset is acquired by the company between 1 April 2002 and 30 June 2020 and either it is acquired from an unrelated party or a related party fulfilling one of conditions A – C as outlined above
3. The asset is acquired by the company on or after 1 July 2020
4. The asset is held by the company immediately before 1 July 2020 and at that time the company is not within the charge to corporation tax in respect of the asset. However, there is anti-avoidance provision whereby this does not apply if the asset is held by any company at any time between 19 March 2020 and 30 June 2020 where that company is within charge to corporation tax

However, it is important to note that the no gain/no loss rules for capital gains within groups of companies is preserved. This means that pre-FA 2002 assets will not come within the IFA regime when they have been transferred intra-group even if that transfer takes place on or after 1 July 2020. Such assets will remain as capital assets.

Further anti-avoidance provisions are introduced which may affect the debits which can be brought into account for tax purposes where the intangible fixed asset is a 'restricted asset'.

A restricted asset is one acquired by the company on or after 1 July 2020 from a related party which falls within one of these categories:

1. The asset was a pre-FA 2002 asset in the hands of any company on 1 July 2020 and at no time on or after 1 July 2020 has the asset been the subject of a 'relieving acquisition' (i.e. an acquisition by a company from a person who is not a related party in relation to the company)

2. The asset was created before 1 April 2002, immediately before 1 July 2020 the asset was held by a person other than a company and at no time on or after 1 July 2020 has the asset been the subject of a relieving acquisition. The asset is not within this section if the vendor (the 'intermediary') acquired the asset on or after 1 April 2002 from a third party who is:
 - a. Not a company or is a company which is not a related party of the intermediary's at the time of the intermediary's acquisition
 - b. The third party is not a related party of a company which is also related to the intermediary
 - c. The third party is not a related party to the company now acquiring the asset
3. The asset is acquired on or after 1 July 2020 and was created after that same date, has not been subject to a relieving acquisition and derives its value from another asset which is a pre-FA2002 asset or a restricted asset in the hand of any company on the date it was created
4. The asset is acquired on or after 1 July 2020 and is acquired directly or indirectly as a consequence of the realisation by another person of another asset where the company and the other person are related parties and the other asset was a pre-FA2002 or restricted asset in the hands of any company between 1 July 2020 and the date of realisation. This only applies if the other asset was not the subject of a relieving acquisition in the same period or after acquisition.

In the first two cases (1. and 2. above), if the company is the first company to acquire the asset on or after 1 July 2020 it is treated as having acquired the asset at no cost for the purposes of the IFA legislation.

If it is not the first company to acquire the asset after that date, the asset is treated as acquired for the 'adjusted amount' which is $A - B$.

- 'A' is the consideration either actually paid or deemed to have been paid
- 'B' is the market value of the asset on the date it was acquired on or after 1 July 2020

If B is greater than A, the adjusted amount is nil.

Where the second two cases apply (3. and 4. above), the asset is also treated as acquired for the 'adjusted amount' but it is a different calculation. This is the consideration either actually paid or deemed to be paid less a just and reasonable apportionment of the 'notional deduction amount' for the other asset. This cannot be a negative number. The legislation which specifies how the notional deduction amount is calculated is complicated but is linked to the market value of the other asset.

There are also extensions to the definition of 'related party' to include circumstances where the participation condition in TIOPA 2010 would be met (i.e. participation in the management, control or capital of another party).

Finally, a company acquiring an asset under an unconditional contract is treated as making the acquisition when the contract is made (or, if later, when it becomes unconditional).

Example

A business, which commenced trading on 1 January 2000 and purchased an intangible fixed asset on 15 January 2001. The business was transferred to a limited company (OldCo) under the same ownership on 1 January 2010.

Even after the FB2020 changes the intangible assets is not going fall within the IFA regime.

The business and assets are sold to a company (NewCo) owned by the same person on 1 April 2021.

Technically the intangible fixed asset comes within the IFA rules as it was purchased by NewCo after 1 July 2020.

However, the asset is a pre-FA 2002 asset in the hands of OldCo on 1 July 2020 and at no time on or after 1 July 2020 has the asset been the subject of a relieving acquisition (i.e. by an unrelated party).

It is therefore a restricted asset which means the acquisition cost for the purposes of the IFA provisions is nil.

The business is then sold to another company owned by the same person on 1 December 2022. The price paid is £1 million and the market value of the asset on 1 April 2021 (when NewCo bought it) was £750,000.

It is still a restricted asset for the same reason as explained in the previous paragraph.

The acquisition price for the purposes of the IFA provisions is (£1m - £750,000) £250,000.

Fungible assets

There is a redefining of the term 'fungible asset'. New s900J explains that fungible assets of the same kind that are held by the same person in the same capacity are treated as indistinguishable parts of a single asset which grows as additional assets are added and diminishes as assets are realised.

In the context of intangible assets, there may be licences that can be bought and sold on a market which have identical characteristics, for example the right to produce or sell a fixed number of units of a product where holding one licences entitles the holder to produce 1 unit, holding two licences entitles the holder to produce 2 units.

In a real life context, when an energy generator produces units of renewable energy they are issued with renewables obligation certificates (ROCs). These can be traded with other parties and are commonly accounted for as intangible assets when purchased.

There are three types of fungible assets:

1. Pre-FA2002 assets
2. Restricted assets
3. Standard intangible fixed assets

These are all to be regarded as assets of different kinds.

This mirrors the legislation as it applied before except that there were only two types of fungible assets before: pre-FA2002 assets and standard intangible fixed assets.

When looking at realisation of fungible assets, there were specific rules which determined which assets were treated as sold where more than one category existed. The basic premise of those rules is retained with the new legislation.

S900L applies where a company realises a fungible asset which would be treated as a single asset but where the legislation treats it as a group of separate assets. The realisation is treated:

1. As diminishing the pre-FA2002 assets first, then
2. Diminishing the restricted assets, then
3. Diminishing the standard IFA

There are also anti-avoidance rules relating to identification of assets. These are similar to the bed and breakfasting rules for shares.

Fungible assets acquired by a company are matched with pre-FA2002 assets or restricted assets realised by the company in the 30-day period either side of the acquisition.

Assets realised earlier are identified before assets realised later. Assets acquired earlier are identified before assets acquired later.

The amendments will apply for accounting periods beginning on or after 1 July 2020, but straddling periods will be treated as split at that date.

Example

A company holds 100,000 units of a fungible asset on 1 April 2020 and buys another 20,000 units on 15 April 2020.

It sells 40,000 units on 1 June 2021 and buys 50,000 units on 15 June 2021. The purchases are from unrelated parties.

It sells 30,000 units on 30 June 2021.

Treatment

Following the 15 April 2020 acquisition, the company is regarded as holding two assets:

1. 100,000 units of pre-FA2002 asset and
2. 20,000 units of standard IFA.

The 40,000 units sold on 1 June 2021 are regarded as diminishing the pre-FA2002 asset in priority so that immediately afterwards the company has 60,000 units of pre-FA2002 asset of and 20,000 of standard IFA.

The 50,000 units acquired on 15 June are regarded as swelling the pre-IFA asset to the extent of 40,000 units under the 30-day 'bed and breakfasting' rule.

As a result, immediately afterwards the company holds 100,000 units of pre-FA2002 asset and 30,000 of standard IFA.

The sale of 30,000 units on June 30 diminishes the pre-FA2002 asset down to 70,000 units.

NR companies with UK property businesses

Finance Act 2019 brings non-resident companies within scope of UK corporation tax from 6 April 2020 if they derive income from UK property.

Clause 31 and Sch.5 of this Finance Bill makes some amendments to those provisions:

The wording of s301(1A) CTA2009 is replaced as it was felt that the previous wording might have limited the taxation of income derived from non-trading loan relationships held in respect of UK permanent establishments of non-UK resident companies. Similar amendments are made to s574(2A) CTA2009 as far as they apply to non-trading derivative contracts.

Pre-6 April 2020 finance costs

A new provision is introduced to make sure that a non-resident company that starts to carry on a UK property business on or after 6 April 2020 can deduct the net amount of financing costs incurred prior to the commencement of the business even if those costs relate to a period before the new regime commenced.

For example, borrowing costs incurred during the construction of buildings in the UK before 6 April 2020, where the company starts to rent the buildings out after this date.

The maximum period over which costs can be deducted is 7 years before the date on which the UK property business commenced. This is in line with other pre-business expenditure provisions.

Similar provisions are introduced in respect of net debits on derivative contracts relevant to the UK property business.

Exception from notifying chargeability to corporation tax

Schedule 5 Finance Act 2019 created an exception from notifying chargeability to corporation tax for non-UK resident companies coming into charge to corporation tax where it was reasonably expected that all its income would suffer income tax deduction at source and it would not have any chargeable gains.

This exception has now been refined so that it becomes conditional on the company having a reasonable expectation that the tax deducted will cover the company's expected corporation tax liability.

Disregard regulations

The Disregard Regulations are amended to provide that the time limits for electing into the Disregard Regs are not accelerated only as a result of a non-UK resident disposing of an asset where the gain is subject to corporation tax.

This will be particularly relevant where the disposal occurs prior to 6 April 2020.

Corporation tax payment plans

Transactions between 75% UK group companies (or between two companies both within the charge to corporation tax) are tax neutral as far as they relate to chargeable assets, loan relationships or derivative contracts.

Clause 33 and Sch.6 of the Finance Bill introduce provisions which defer the payment of tax under a corporation tax payment plan for these transactions where the transferor is a UK company and the transferee is a resident outside the UK in an EEA state and outside the charge to UK corporation tax in respect of the transferred item after the transaction.

The transfers to which this applies are:

- Those within s171 or s139 TCGA 1992 (intra-group transfers of chargeable assets or qualifying reconstructions);
- Those within s340(3) CTA2009 (replacement of one group company by another as a party to a loan relationship) or s625(3) CTA2009 (the same but in relation to derivative contracts)
- Those within s775 CTA2009 (intra-group transfers of intangible fixed assets).

The tax which qualifies to be part of a corporation tax payment plan is the difference between the amount due and the amount which would have been due if one of those provisions had applied.

A single payment plan applies for an accounting period regardless of the number of transactions involved and the company must apply within nine months of the end of the accounting period.

The company is undertaking to pay the tax deferred plus any interest. Acceptance of this by HMRC may involve requesting of security by HMRC if they feel there is a serious risk to the collection of the tax.

The payment plan involve the tax that has been deferred being paid in six annual instalments, commencing nine months after the accounting period in which the disposal occurred. The whole of the balance of the deferred tax become payable on the occurrence of a qualifying event.

These include the company that entered into the plan:

- Becoming insolvent
- Appointing a liquidator or administrator
- Failing to make payments due for a period of twelve months after they become due
- Ceasing to be within charge to UK corporation tax

Or the transferee company:

- Ceasing to be resident in an EEA state
- Ceasing to be a member of the same group as the transferor company
- Selling or otherwise disposing of the item subject to the transaction.

There are various penalties for failure to comply with these provisions.

The provisions come into force on 11 July 2019 and can apply for a qualifying transaction in any period ended on or after 10 October 2018.

Accounting standards affecting leases

There were significant provisions in FA2019 relating to the introduction of IFRS16 which is an accounting standard relating to leases.

Clause 34 amends Sch.14 FA2019 to clarify that the spreading rules in Sch.14 apply to all lessees adopting International Financial Reporting Standard 16 (IFRS 16) for any period of account, including periods commencing before 1 January 2019. The amendment is treated as always having had effect.

Where a lessee has adopted IFRS 16 for a period of account beginning before 1 January 2019, the transitional provisions in paragraph 13, Sch. 14 FA2019 have effect as if IFRS 16 were adopted in the first period of account beginning on or after 1 January 2019. This makes the calculation of the transitional deduction or taxable amount more difficult to calculate.