

Corporation tax rates (Lecture B1251 – 16.53 minutes)

Main rate of corporation tax

For 2021 and 2022, the main rate of corporation tax (for non-ring-fenced profits) will remain at 19% (Clause 6(2)(a)).

From 1 April 2023, this rate will increase to 25% for companies with augmented profits (see below) over £250,000 (Clause 6(2)(b) or whose profits are ring fence profits (from production and sale of hydrocarbons in the North Sea).

The 25% rate will also apply to Real Estate Investment Trusts whose profits and/or gains arising from its residual business are charged to corporation tax, as well as open-ended investment companies (OEICs) and authorised unit trusts.

Small profits rate

Companies with augmented profits of £50,000 or less will continue to be taxed at 19% (Clause 7(2)(a)).

Close investment-holding companies

A close investment-holding company will pay tax at the main rate of 25% from 1 April 2023. A close company will be a close investment-holding company unless it exists

1. To carry on a trade or trades on a commercial basis, or
2. To invest in land or estates in land for letting commercially, or
3. To hold shares and securities of, or to lend money to companies which are qualifying companies or is an intermediate holding company of a trading/letting group, or
4. To co-ordinate the administration of two or more qualifying companies (i.e. a management services company) or to make the investment in land for a qualifying company or its parent company.

Letting commercially is any letting unless the tenant is a person connected to the company or their spouse, civil partner or relative (plus the spouse's or civil partner's relatives and their spouses and civil partners).

If a company is wound up and was not a close investment-holding company in the accounting period immediately before winding up commences, it is not treated as a close investment-holding company in the winding up period (e.g. if the liquidator had sold its trade or investment property).

Non-resident companies

Non-resident companies are not eligible to use the small profits rate, nor are they entitled to marginal relief. This means that they will be liable to 25% corporation tax on their UK profits chargeable.

This would cover UK permanent establishments and UK property business profits of non-resident companies.

Controlled foreign companies

Part 9A TIOPA 2010 charges UK resident companies corporation tax on their share of the profits of controlled foreign companies in some circumstances.

From 1 April 2023, the tax charged will be at 25% as the TIOPA 2010 legislation refers to the 'main rate'.

Augmented profits

Augmented profits are the profits chargeable to corporation tax plus any exempt distributions of a qualifying kind received by the company that are not excluded (future s18L CTA 2010).

An exempt distribution of a qualifying kind is a distribution for corporation tax purposes because (and only because) it falls within paras A, B, G or H of s1000(1). This includes not only regular dividends, but also other distributions in respect of shares, the transfer of assets or liabilities treated as distributions in specie and bonus issues following repayment of share capital.

Dividends received from subsidiaries or other group companies of which the recipient is a 51% group company are excluded.

For this purpose, "A" is a 51% subsidiary of "B" if

1. B beneficially owns (directly or indirectly) more than 50% of the ordinary share capital of the subsidiary, and
2. B is entitled more than 50% of the profits available for distribution to the equity holders of B, and
3. B would be beneficially entitled to more than 50% of the assets of A available for distribution to its equity holders on a winding up

Shares owned indirectly for trading purposes by other group companies are ignored.

Dividends received from

1. a trading company (i.e. it wholly or mainly carries on one or more trades), or
2. a relevant holding company (i.e. it wholly or mainly holds shares in, or securities of, 90% trading subsidiaries)

which is a 'quasi-subsiary' of the recipient company are also excluded.

A quasi-subsiary is one owned by a consortium in which the recipient of the dividends is a member but is not a 75% subsidiary of any company and there is no arrangement by which it could become a 75% subsidiary of any company.

A company is owned by a consortium if at least 75% of its ordinary share capital is beneficially owned by at least two companies, each of which

1. owns at least 5%, and
2. would be entitled to
 - at least 5% of the dividends available for distribution to equity holders, and

- at least 5% of the assets available to equity holders on a winding up.

Marginal relief

Schedule 1 re-introduces the rules on marginal relief that existed until 31 March 2017.

Where augmented profits fall between £50,000 and £250,000, the tax rate will be 25%, but companies will be able to claim marginal relief.

The marginal relief is calculated as:

$$\text{MR fraction} \times (\text{Upper profit limit} - \text{Augmented profits}) \times \frac{\text{Taxable profits}}{\text{Augmented profits}}$$

The profit limits will be divided by the number of *associated companies* (not the number of 51% group companies).

The limits are also reduced if the chargeable accounting period is less than 12 months.

The marginal relief fraction will be 3/200ths (Clause 7)(2)(b)) and the marginal rate of tax between the lower and upper limit will be 26.5% in the absence of any dividend income. If the company has relevant dividend income, the marginal rate of tax between the lower and upper limits is even higher than this.

There are special rules for calculating marginal relief where a company has both ring-fence and non-ring-fence profits; these ensure that the marginal relief only applies, where applicable, to non-ring fence profits.

Associated companies

A company (whether UK resident or not) is associated with another company at a particular time if, at that time in the chargeable accounting period

- a) One company has control of the other, or
- b) Both companies are under the control of the same person or group of persons.

Control is defined in s451 CTA 2010. It exists where a person exercises, or can exercise, or can acquire direct or indirect control over a company's affairs. This includes where the person owns or can acquire

1. More than 50% of the share capital or issued share capital, or
2. The majority of the voting rights, or
3. Entitlement to the majority of the distributable profits, or
4. Entitlement to more than 50% of the assets available for distribution to participators

This includes situations where two or more persons together satisfy the conditions above.

If there is no substantial commercial interdependence between the companies, the normal attribution of rights held by certain connected persons (s451 CTA 2010) is ignored. Regulations will

prescribe the factors that constitute substantial commercial interdependence but in the past these have consisted of financial, economic and organisational links between the companies.

Business partners' shares have, in the past, caused problems with the small profit rate. Where director/shareholders of a company have entered into tax avoidance schemes that involved being a member of an LLP, they may have had no idea who their fellow members were, but they still counted as business partners.

If each of these partners owned their own companies, then the companies were associated. It was often impossible to calculate the number of associate companies in this situation, so each company had to pay tax at the main rate.

It is expected that the same issues will arise from 1 April 2023.

Fixed-rate preference shares held by a company are ignored if the holder is not a close company, takes no part in managing the issuer and subscribed for the shares in the ordinary course of a business which includes the provision of finance.

Association through a loan creditor

A company is not under the control of its lender if there is no other connection and either the lender is not a close company or its relationship with the borrower arose in the ordinary course of the lender's business.

This applies equally for two companies controlled by the same lender only by virtue of the amounts lent to them.

Exclusions

Companies that have not carried on a trade or business at any time in the accounting period (or for the part for which they were associated) are ignored.

This includes 'passive' holding companies that do not carry on a trade and which hold at least one 51% subsidiary.

A passive company

1. Has no assets in the period apart from shares in 51% subsidiaries;
2. Has no income in the period other than exempt dividends of a qualifying kind, as defined above;
3. Has no chargeable gains in the period (the disposal of its subsidiaries will be exempt if they meet the conditions for substantial shareholdings exemption);
4. Has no expenses of management in the period;
5. Did not make any deductible charitable donations in the period; and
6. Redistributes at least the amount of dividend income in the period to at least one shareholder

If exempt dividend income arises, any asset representing it is not treated as an asset for the purpose of 1. above, so that it would not breach the conditions for the company to be excluded.

This would be the case where the company accrues the dividend because the subsidiary has legally declared it payable but hasn't paid it to the company by the end of the period.

Examples

Example 1 – single company, no dividend income

ABC Limited has a year ended 31 March 2024. It has chargeable profits of £190,000 and no dividend income.

In this case the taxable profit and augmented profit are both £190,000.

As the profit is between the lower profit limit of £50,000 and the upper limit of £250,000, marginal relief applies.

Its corporation tax liability for the year will be:

	£
Tax at 25% on £190,000	47,500
Minus: $\frac{3}{200} \times (250,000 - 190,000) \times 190,000 \div 190,000$	<u>(900)</u>
	<u>46,600</u>

This could also be calculated as:

	£
First £50,000 taxable at 19%	9,500
Remaining £140,000 taxable at 26.5%	<u>37,100</u>
	<u>46,600</u>

Example 2 – single company, exempt dividend income

DEF Limited has a year ended 31 March 2024. It has chargeable profits of £190,000 and foreign dividend income from a non-group company of £50,000 which is net of 5% withholding tax deducted by the payer.

In this case, the taxable profit is £190,000 and the augmented profit is £240,000 (we include the dividend received as the withholding tax is irrecoverable).

Its corporation tax liability for the year will be:

	£
Tax at 25% on £190,000	47,500.00
Minus: $\frac{3}{200} \times (250,000 - 240,000) \times 190,000 \div 240,000$	<u>(118.75)</u>
	<u>47,381.25</u>

The marginal rate of tax on the excess profit above £50,000 is greater than 26.5% as a result of the foreign dividends.

	£
£50,000 @ 19%	9,500.00
£140,000 @ 27.058% (balancing rate)	<u>37,881.25</u> (balance)
	<u>47,381.25</u>

Example 3 – single company, exempt dividend income

DEF Limited has a year ended 31 December 2023. It has chargeable profits of £190,000 and foreign dividend income from a non-group company of £50,000 net of 5% withholding tax deducted by the payer.

Again, the taxable profits are £190,000 and the augmented profits are £240,000.

Its corporation tax liability for the year will be:

	£
<u>1 January 2023 – 31 March 2023:</u>	
(£190,000 x 90 ÷ 365) = £46,849 x 19% =	8,901.31
<u>1 April 2023 – 31 December 2023:</u>	
Upper limit = 250,000 x 275 ÷ 365 = £188,356	
Taxable profits = 190,000 x 275 ÷ 365 = £143,151	
Augmented profit = 240,000 x 275 ÷ 365 = £180,822	
Tax: £143,151 x 25%	35,787.75
Minus: 3/200ths x (188,356 – 180,822) x 143,151 ÷ 180,822	<u>(89.47)</u>
	<u>44,599.59</u>

Example 4 – group of companies

GHI Holdings Limited is the parent company of a multi-company group. There are 9 subsidiaries, 3 of which are non-UK resident trading companies, 2 are dormant and the remaining 4 are UK resident trading companies.

GHI Holdings does not trade itself. It is a pure holding company, receiving dividends from its subsidiaries and paying these on to its shareholders. It incurs no other expenditure and has no assets apart from its shareholdings in subsidiaries.

The four UK resident trading companies have the following taxable profits for the year ended 31 March 2024:

JKL Limited	£140,200
MNO Limited	£24,450
PQR Limited	£6,420
STU Limited	£78,110

None of the four subsidiaries receives any dividend income.

Analysis

The lower and upper profit limits need to be divided by the number of associated companies. GHI Holdings Limited is excluded as are the two dormant subsidiaries, so the limits need to be divided by 7 (the 4 UK resident trading companies and the 3 non-UK resident trading companies).

The lower limit is therefore £7,143 and the upper limits £35,714.

This means that JKL Limited and STU Limited will pay tax at the main rate of 25%. PQR Limited will pay tax at the small company rate of 19% and MNO Limited will be eligible for marginal relief.

Their tax liabilities will therefore be:

JKL Limited: 25% x £140,200	<u>£35,050.00</u>
MNO Limited: 25% x £24,450	6112.50
Minus: $3/200 \times (35,714 - 24,450)$	<u>(168.96)</u>
	<u>£5,943.54</u>
PQR Limited: 19% x £6,420	<u>£1,219.80</u>
STU Limited: 25% x £78,110	<u>£19,527.50</u>

Consequential amendments

Corporation tax instalment payments

The Corporation Tax (Instalment Payments) Regulations 1998 will be amended for accounting periods beginning on or after 1 April 2023.

The £1.5 million and £20 million profit limits for testing whether a company has to make quarterly instalment payments will be divided by the number of associated companies, rather than the number of 51% group companies.

This may cause some companies that are under the common control of natural persons to become liable to pay tax by instalments. However, in the first year that this happens, the 'grace period' provisions should delay the instalments until the following accounting period.

Regulation 3 of The Corporation Tax (Instalment Payments) Regulations 1998 (SI 1998/3175) states that a company is not a large company for this purposes if

- a) Its profits do not exceed £10,000,000, and
- b) Its was not a large company in the twelve months prior to this accounting period

Example

Adam Chan owns 100% of AC Properties Limited and 100% of AC Consultancy Limited. Both companies have made profits in their year ended 31 March 2021 accounts in the region of £1 million to £1.2 million and are expected to do so for the foreseeable future.

Explain when these companies will need to pay their corporation tax over the next 3 years.

Analysis

Accounting period	Corporation tax payment date(s)
Year ended 31 March 2021	1 January 2022
Year ended 31 March 2022	1 January 2023
Year ended 31 March 2023	1 January 2024
Year ended 31 March 2024	1 January 2025
Year ended 31 March 2025	14 October 2024 (25%), 14 January 2025 (25%), 14 April 2025 (25%), 14 July 2025(25%)

The profit limit for quarterly instalments for the year ended 31 March 2024 is (£1.5m ÷ 2) £750,000, so both companies exceed the profit limit for instalment payments. However, they were not large companies in the previous 12 months (when we only consider 51% group companies, so each was not large if its individual profit was less than £1.5 million), so instalment payments will not commence until the following year.

The first instalment of tax for year ended 31 March 2025 is due before the tax for the previous year and the second instalment is due two weeks after the due date of the tax for the previous year. This advancement of cash outflows will need to be budgeted for and managed well in advance of them falling due to avoid any financial distress.

Long-life assets

The monetary limit in s99 CAA 2001 of up to £100,000 for which expenditure is excluded from being a long-life asset will be divided by the number of associated companies rather than the number of related 51% group companies for accounting periods beginning on or after 1 April 2023.

Patent box small claims treatment

S357BN CTA 2010 permits a company to make some simplifying elections when calculating its patent box deduction. These are a notional royalty election (s357BNA), a small claims figure election (s357BNB) and a global streaming election (s357BNC).

To qualify to make these elections, the qualifying residual profit of the trade for an accounting period must not exceed the greater of

1. £1,000,000 and
2. The relevant maximum for the accounting period

The relevant maximum for an accounting period for a company which is not part of a group is £3,000,000.

This is currently divided by the number of related 51% group companies. For accounting periods beginning on or after 1 April 2023, it will be changed to the number of associated companies.

Insurance companies carrying on long-term business

S102 FA2012 is amended so that the policyholders' share of the I – E profit from 1 April 2023 is omitted in determining the augmented profits and taxable total profits of the company for the accounting period, for the purpose of determining if the company has small profits.