Corporate Tax Issues and Opportunities in 2018
Reporting gathers pace

This is resulting in a wave of local and international reporting obligations. In 2017 the UK draft finance bill was the largest on record running to 762 pages, while new international reporting requirements including the OECD’s Country by Country Reporting came into effect for accounting periods starting on and after 1 January 2016, with the first submissions taking place in December 2017. Additionally, May 2017 saw the first UK submissions under the OECD’s Common Reporting Standard (CRS) which requires financial institutions, including banks, to report on the tax residency of their customers. The list of participating CRS countries has doubled, with a total of 102 countries now reporting details of accounts for calendar year 2018.

On top of this HMRC’s Making Tax Digital (MTD) initiative will soon apply to companies. The VAT element of MTD is due to apply to VAT registered companies with annual turnover of £85,000 or more from 1 April 2019. The corporation tax element of MTD has not been legislated for as yet but it is expected to apply from April 2020 and may result in a four-fold increase in corporate tax reporting obligations - See What’s on the radar below.

With all this going on we thought it would be helpful to pick out the key changes we are seeing in Corporation Tax obligations in 2018 and what is on the near horizon.

“The corporation tax element of MTD... is expected to apply from April 2020 and may result in a four-fold increase in corporate tax reporting obligation”
The current changes which tax practitioners and in-house tax managers have to get to grips with can be divided into:

- the good - more flexibility in the use of losses, and easier tax rules when selling subsidiaries
- the bad - restrictions on relief for carried forward losses, and interest paid
- the ugly - new criminal offences for tax evasion.

Here’s what these developments mean in greater detail:

**Losses**

The rules concerning the use of corporate losses have been shaken up from 1 April 2017. The most radical change is that the old restrictions about setting carried forward trading losses against profits from the same trade are swept away.

Carried forward losses arising from all income types (e.g. trading, intangibles, loan relationships, property income, excess management expenses) can now be set against the company’s entire taxable profits for future periods, or may be surrendered as group relief to other companies within the group. Furthermore, for the first time, the company has a discretion as to how much of the carried forward losses it sets against the total profits of any particular year. Subject to the restrictions below, it may relieve only part of the losses, carrying forward any surplus to future years – it may even decide not to claim any relief for the year in question. However, the company needs to be careful to claim an amount of losses carried forward and brought forward on every applicable corporate tax return, as missing such a claim could mean the ability to use the loss disappears.

There are also some new restrictions where the profits of the company or the group are over £5m. In that case carried forward losses are freely available to set against the first £5m, but are capped by 50% of the excess. These restrictions apply to both trading and non-trading losses and include those losses which arose before April 2017. The calculation of the amount of the restriction is complex, including a new definition of profits available for the purposes of relief and with allocation of the £5m allowance potentially creating tax efficiencies, and must be performed correctly to be acceptable to HMRC. Many practitioners will rely on tax software to get the result of this calculation right.

This new flexibility for post April 2017 losses means that it may be advantageous for a loss to arise later, or to use existing pre-April 2017 losses earlier. The tax computation for periods ending on 31 March 2017 can be amended until 31 March 2019, to make or eliminate claims for large deductions such as R&D relief.

**Selling companies**

Groups of companies have been able to sell trading subsidiaries with no tax due on the gains made since April 2002, if the conditions for the substantial shareholdings exemption (SSE) are met. From 1 April 2017 the SSE conditions have been relaxed, so that many more share disposals can qualify and be free of tax.

A significant change is that the vendor company no longer has to be a trading company or a member of a trading group, either before or after the sale of the subsidiary. Also, in most situations, the company which is disposed of doesn’t have to be a trading company immediately after the disposal. In addition, the relief is extended to non-trading companies of groups where at least 25% of the vendor company’s ordinary share capital is held by qualifying institutional investors. All these changes allow the SSE to be claimed by mixed trading and investment groups, and thus make the exemption available to a wider range of businesses.

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Interest relief

Some international corporate groups pay interest in high-tax regimes, and receive interest in low tax regimes, and thus take advantage of differing tax rates around the globe. As part of the drive by the OECD and the G20 countries to tackle base erosion and profit shifting (BEPS), the UK has restricted the deduction of interest for group return periods starting on or after 1 April 2017.

These new rules only apply where the group of companies has a net tax interest expense for the year of more than £2m. This is broadly the total interest paid less the total interest received in the period, but “interest” is widely defined to include amounts economically equivalent to interest.

The group must compare its net tax interest expense with an interest allowance, which is generally calculated as 30% of the group’s EBITDA (earnings before interest, tax, depreciation and amortisation). Where tax interest expense is excessive, a total disallowed amount arises and this must be allocated between the group companies as they see fit. The allocated amount must be disallowed for tax purposes, thus increasing the company’s taxable profits.

The group needs to keep a record of the interest allowance it has used, as unused allowance may be carried forward to use in later years. Also amounts of interest disallowed by a company may be reactivated in later years, but this disallowed amount is attached to the individual company.You can see that these restriction of interest rules involve a lot of precise record keeping and form filling!

Criminal offence of tax evasion

On 30 September 2017 it became a criminal offence to fail to prevent tax evasion, as defined in the Criminal Finances Act 2017. The law is designed to pin the blame for tax evasion on large multi-national organisations who can’t easily be called to account, but it applies to any incorporated body or partnership. The law does not extend to the responsibilities of individuals, unless they are acting for a business.

The business is vicariously liable if an employee or other associated person criminally facilitates tax evasion whilst acting in that capacity for the business, even if the senior management of the business was not involved or aware of what was going on. Tax evasion in this context is the fraudulent evasion of UK taxes or overseas taxes by a taxpayer (an individual or legal entity), under existing law.

The consequences for breaching the Act include unlimited financial penalties, confiscation orders, serious crime prevention orders, regulatory issues and reputational damage.

The main line of defence is for the business to have reasonable procedures in place to prevent the facilitation of tax evasion, or that it was not reasonable in the circumstances to expect there to be a procedure in place. The advice for businesses and the tax advisers working with those businesses is to conduct risk assessments and put in place proportionate prevention controls and procedures.

The types of businesses most at risk are those which pay large sums to consultants, do cross-border business, engage casual or itinerant labour and contractors, or handle goods and services where organised fraud is a risk. All corporate boards need to discuss this issue to show the company has written policies in place to counter acts such as; falsifying dates on dividend documents, or claiming for non-deductible expenses.
Regular changes

The tax law is changed regularly in small ways, which all need to be noted and acted on. Here are a few of those smaller issues which will affect your company in the next 12 months:

Tax rates

The current corporation tax rate of 19% applies to all companies except for companies in the oil and gas sector, which pay tax at a main rate of 30% or at a small profits rate of 19%, on ring fenced profits.

This standard rate of corporate tax is due to drop from 19% to 17% on 1 April 2020. Before that date companies trading in Northern Ireland could benefit from a special rate of corporation tax, which is expected to be set at 12.5%, to match the rate in the Republic of Ireland. However, the UK Government has said the power to change the corporation tax rate won’t be devolved to the Northern Ireland Executive until it demonstrates its finances are on a sustainable footing.

R&D reliefs

Research and development (R&D) tax relief is given in a different manner for SME companies and large companies. “Large” in this context means companies with more than 500 employees and turnover of €100m or more, or with a balance sheet value which is €86m or more. Those limits are defined in Euros in the legislation. All other companies are SMEs.

SME companies claim R&D relief as an enhanced deduction of 230% of the qualifying costs, so for every £100 of R&D costs, the company claims £230 as a deduction the calculation of taxable profits. Where the SME company undertakes R&D work as a subcontractor to a large company it can claim R&D tax relief using the RDEC method.

Patents

Where the company owns, or holds an exclusive licence for, patents issued by the UK Intellectual Property Office, European Patent Office or a number of other countries, it can pay 10% corporation tax on profits attributable to those patents. Profits from creating or developing the patented product, or a product containing the patented item, qualify for this reduced rate of corporation tax. Profits from holding patents as investments do not qualify.

Costs and revenues should be streamed on a patent-by-patent or product-by-product basis, although this streaming treatment is being phased in for companies which were already claiming Patent Box treatment before 1 July 2016. These streaming rules are amended where R&D projects are undertaken collaboratively by two or more companies under a cost sharing arrangement from April 2017 onwards.

The election for this Patent Box treatment must be made within two years from the end of the accounting period in which the profits arose.

“RDEC increased from 11% to 12%”
Creative industries

If your company produces British films, TV programmes, theatre productions, orchestra productions, museum exhibitions or video games, don’t forget to investigate whether it qualifies for one of the special creative industry tax reliefs. These can provide additional tax deductions of 100% of the core production expenditure. Where a loss is made up to 25% of that loss can be surrendered for a payable tax credit. The claim must be made within the corporation tax return or by amending that return within one year of the final filing date for that return.

Capital allowances

The rates of capital allowances have not been altered since 2012, these are: 18% for assets in the main pool and 8% for asset in the special rate pool. However, the conditions for assets to qualify for the 100% first year allowance (FYA) have changed.

Cars qualify for the FYA of 100% only where the vehicle is purchased new and unused, and it has low CO2 emissions. For cars purchased from 1 April 2015 to 31 March 2018, the CO2 emissions must be no more than 75g/km to count as “low emissions”. From 1 April 2018 the emissions threshold has been reduced to 50g/km.

This does mean 100% allowances can be claimed for all electric cars. Also the cost of any electric vehicle charging points qualify for 100% allowances where cost is incurred by 31 March 2019. Refuelling stations for gas powered vehicles qualify for 100% FYA if the cost is incurred by 31 March 2021.
Year-end checks

As your accounting year comes to a close it’s good opportunity to tidy-up loose ends. Here is a list of the key tax-related areas to review:

**Pension contributions**

Where pension contributions are payable for employees or directors those amounts need to be actually paid with the accounting period to be a deductible expense for the period. An accrued pension liability will only be tax deductible in the period it is actually paid.

However, accrual salary and bonuses can be deducted for tax purposes if the amount due is actually paid within nine months of the accounting period end.

**Loans to participators**

A close company can be liable to pay an extra corporation tax charge of 32.5% of the value of loans it has advanced to participators or associates of a participator in the company. A close company is one which is controlled by five or few of its participators or by its directors. The level of the company’s turnover or profits are irrelevant for this test.

The charge applies if the loan is still outstanding nine months after the end of the accounting period in which the amount was first borrowed. So the tax charge can be avoided if the loan is repaid within that nine-month period. But where a loan of £5,000 or more is repaid and re-advanced within 30 days to the same borrower or his associates, it is treated as continuing, ignoring the temporary repayment. If the loan is for £15,000 or more and arrangements are in place for the borrower (or an associate) to take a replacement loan from the company an amount of £5,000 or more, the loan will be treated as continuing if the replacement loan is made at any time.

**Annual investment allowance**

Capital allowances must be claimed within two years of the end of the accounting period in which the expenditure was incurred. Expenditure on plant and machinery will generally be covered by the annual investment allowance of £200,000 per year for expenditure incurred from 2016 onwards.

Where the company has acquired a property from April 2012 onwards, that contains fixtures or equipment, it’s important to match any claim for capital allowances on those items, with the values agreed on the acquisition. The previous owner of the property must show that the items were included in a capital allowance pool, for the subsequent owner to claim further allowances.

**Diverted profits tax**

Companies with profits of at least £10m, or expenses of at least £1m, in the UK need to check whether the diverted profits tax (DPT) could apply to those business carried on in the UK. The DPT is set at 25% of the amount HMRC concluded has been diverted, or 55% for diverted profits in the oil and gas industry.
What's on the radar?

**MTD for corporation tax**

We don’t yet know what the obligations to report corporation tax under MTD will entail, but it is likely to be a quarterly reporting regime to replace the current annual corporate tax return. Companies will be required to keep accounting records digitally and to submit reports to HMRC using an API embedded in accounting software. HMRC has said it has no plans to change the payments of corporation tax for the majority of companies to align with quarterly reporting under MTD. Companies will need to look at their resourcing plans and budgets to allow for extra workloads.

**Tax payment dates**

For accounting periods starting on and after 1 April 2019, where the annual profits of the company or group exceed £20 million, the corporation tax due will be payable in four instalments at the following intervals:

- 1st: 2 months and 13 days from the start of the accounting period (or date of final instalment, if earlier)
- 2nd: 3 months after 1st instalment
- 3rd: 3 months after 2nd instalment
- 4th and final: 3 months after 3rd instalment.

This represents an acceleration in payment dates of 4 months on the current payment dates for large companies with annual taxable profits of £1.5 million or more.
Summary

The increasing number of reports needed for the different corporate taxes and reliefs together with Making Tax Digital on the near horizon mean that tax professionals will increasingly spend large amounts of time on manual data collection, often having to engage with multiple departments and accounting systems to get the tax data they need. All this data must be reviewed for quality and integrity, reworking and then consolidating into the form suitable for reporting to HMRC.

These time-consuming tasks will increasingly tie down skilled staff who could be more productively engaged on value-added activities such as tax planning and risk assessment. The challenges presented by the new flexibility in the use of losses, interest set-off and SSE, for example, will require the attention of experienced tax practitioners.

Organisations should explore the opportunity to free internal tax expertise to concentrate on high value tax planning by installing automated solutions for end-to-end processes for the collection, cleansing and storage of financial data, and creation and preparation of tax computations. For organisations with complex tax affairs these automated software systems can then be overlaid with dashboards allowing for improved control of risk and the management of processes.

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About Tax Systems

Tax Systems is a leading specialist in corporation tax technology and services in the UK and Ireland. Our solutions automate the end-to-end compliance process, reduce operational risks in the process and increase process intelligence so that expert professionals are able to focus on delivering more value to their business or clients.

Tax compliance and reporting is moving at a rapid pace. Tax regulators are focused on increasing tax revenues, reducing tax evasion and ensuring businesses are paying their fair share to support government spending and reduce annual deficits without the need to raise taxes. This is resulting in a wave of local and international reporting obligations, alongside demands for increased tax transparency, at a time when tax team resources are stretched and internal stakeholders are demanding ever more value from their tax professionals. With traditional manual approaches struggling to cope with the scale of the challenge, organisations are having to increase the efficiency of their teams by embracing technology to automate processes and identify areas of improvements whilst reducing risk and creating more effective collaboration with advisors.

Our objective at Tax Systems is to help organisations meet this challenge by providing proven and innovative technology and services delivered by a close-knit team with rare skills and capabilities in both tax and technology, all of which are based locally in the UK and Ireland.

Our solutions enable customers to automate their end-to-end compliance processes from the collection and management of financial data, sensitisation of tax data, creation of computations, statutory report generation and control of associated processes and risk. We collaborate closely with our customers to help them embrace technology to reap the benefits of increased accuracy, auditability, control and efficiency of reporting, as well as saving time associated with manual compliance processes. We aim to change the nature of relationships between advisors and corporates by freeing up skilled resources to focus on adding strategic value to their organisations.

Tax Systems is a public company quoted on the AIM market of the London Stock Exchange with offices in Dublin, Farnham and Staines. Tax Systems is the creator of Alphatax, the market leading corporation tax compliance software built over the last 25 years with a £60 million investment into research and development. Alphatax is used by over 1,000 customers including 43% of the UK FTSE 100 and 23 of the top 25 Accountancy firms.
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