CHAPTER 28

CLOSE COMPANY IMPLICATIONS – PART 1

28.1 Introduction

Close company rules exist to prevent shareholders and directors of close companies from using those companies as an extension to their own private banking facilities without paying any tax! Rules exist with regard to:

- **loans to participators** and
- **benefits provided to participators**.

28.2 Loans to participators

Jack is both a director and shareholder of Vine Ltd. Within the company's books Jack is likely to have a current account, where amounts he is entitled to from the company are credited and amounts he takes out are debited. CTA 2010, s.455

Jack is entitled to a salary, after tax, of £80,000. The company will debit salary costs and credit Jack's current account. The salary itself is taxed as earnings using the PAYE system.

Jack is also entitled to dividends from the company of £50,000. The company will debit dividends and credit Jack's current account. The dividends themselves will be taxed on Jack at the usual dividend rates and higher rate tax may be due.

We can see that Jack is entitled to withdraw a total of £130,000 from the company. Assume that Jack actually takes out £150,000. Jack has borrowed an extra £20,000 from the company by way of a "loan to a participator".

It is this loan that the close company rules seek to tax under the provisions of CTA 2010, s.455.

28.3 S.455 tax

Close companies which are not liable to pay their corporation tax by instalments will be required to pay **s.455 tax on their normal due date, i.e. 9 months and 1 day** following the end of the chargeable accounting period. CTA 2010, s.455(3)

The **tax is calculated as 25% of the loan** and is payable by the company.

The **amount of the loan** is taken as the **lower of the amount outstanding on**

- **the last day of the chargeable accounting period** or
- **the normal due date.**

For larger close companies s. 455 tax is added to the amount of tax due by instalments which adds a horrendous complication to the instalments system!

Example 1

Jack borrowed £20,000 from Vine Ltd (a small close company) on 30 September 2009. He will repay it as follows:

30.9.10	Repaid £10,000
30.9.11	Repaid £5,000
30.9.12	Repaid £5,000

Vine Ltd has a 31 December accounting date.

How much tax is due under s.455 and when is it due?

28.4 Repayment of s.455 tax

Where the loan is either repaid by the participator or waived by the company (in other words written off, with the participator being released from any further repayments), tax previously paid under section 455 will be refunded back to the company.

The **refund** is **made by reducing the company's tax liability for the chargeable accounting period in which the loan is repaid or waived.** Claims for relief under s458 should be made within 4 years of the end of that accounting period. As most close companies are small, this will normally be nine months and one day from the end of the accounting period in which the repayment or release of the loan is made. CTA 2010, s.458(1)

Example 2

In the previous example, Vine Ltd paid s.455 tax of £2,500 on 1.10.10 in respect of a loan outstanding of £10,000.

The loan is repaid as follows:

30.9.11	£5,000
30.9.12	£5,000

How much s.455 tax will be refunded to Vine Ltd and when?

28.5 Implications for the participator

If a company waives a loan to a participator the company will receive a repayment of the s.455 tax. The individual has received real money from the company. The **participator** therefore **will be treated as receiving a dividend equal to the amount of the loan waived**. ITTOIA 2005, s.415(1)

The date of receipt of the dividend will be the date of the loan waiver. An individual will pay higher rate tax via self assessment if he is a higher rate taxpayer.

Illustration 1

Heppel Ltd, a small close company, advanced £15,000 to Fred, who is a director and shareholder, on 31 December 2008.

On 31 December 2010 Fred repaid £5,000 and Heppel Ltd waived a further £9,000.

Heppel Ltd has a 31 March year end.

Implications for Heppel Ltd:

The loan is advanced on 31 December 2008, which is in the company's accounting period ended 31 March 2009.

S.455 tax is due nine months and one day later, on 1 January 2010:

25% x £15,000 = £3,750

This tax is refunded when the loan is either waived or repaid. A total of £14,000 is released from the loan on 31 December 2010, which is during the company's year ended 31 March 2011.

Any refund is made nine months and one day later, on 1 January 2012:

25% x £14,000 = £3,500

Implications for Fred:

Fred is deemed to receive a dividend of £9,000 on 31 December 2010, which is in tax year 2010/11. Assuming that Fred pays tax at 50%, he will be taxed on that dividend. The dividend itself is grossed up for the tax credit of 10%.

	£
$£9{,}000 \times \frac{100}{90}$	10,000
Tax at 42.5%	4,250
Tax credit: £10,000 x 10%	(1,000)
Higher rate tax due	3,250

This tax will be due on 31 January 2012.

Answer 1

Loan advanced 30.9.09 which is during the company's year end 31.12.09

Amount outstanding:
At end of CAP i.e. at 31.12.09 = £20,000
At due date of payment for CT i.e. at 1.10.10 = £10,000

So the s.455 tax due on 1.10.10 is:

£10,000 x 25% = £2,500

Answer 2

First repayment on 30.9.11 is during the company's year ended 31.12.11

Refund made on 1.10.12 is:

£5,000 x 25% = £1,250

Second repayment on 30.9.12 is during the company's year ended 31.12.12

Refund made on 1.10.13 is:

£5,000 x 25% = £1,250