

CHAPTER 29

CLOSE COMPANY IMPLICATIONS - PART 2

29.1 Loans excluded from s.455 Charge

[CTA 2010,
s.456](#)

Loans made in the ordinary course of business of the company are excluded from the s.455 charge. Under this exclusion the close company must be a bank or similar moneylender.

In *Brennan v Deanby Investment Company Limited* the company made a series of loans to its Chairman and one other loan to an independent person. It was held in this case that, although the Chairman was paying commercial interest to the company on the loans, s.419 ICTA (as was, now s.455 CTA 2010)) still applied because the making of a number of different loans to the same connected person did not constitute the business of a moneylender and the company therefore lost its appeal.

There is also an exclusion for the supply of goods or services in the ordinary course of the trade unless the credit period is longer than normal.

[CTA 2010,
s.456\(2\)](#)

There is also an exclusion for loans of no more than £15,000 made to a full-time director or employee who is entitled to no more than 5% of the company's assets on a winding-up. When calculating this 5%, we must also take account of holdings owned by his associates.

[CTA 2010,
s.456\(3\)-
\(6\)](#)

But if the borrower acquires a 5% holding at a time when the whole or part of the loan remains outstanding, then he will be treated as receiving a loan at that time.

[CTA 2010,
s.456\(7\)](#)

Illustration 1

Green Ltd, a close company with a December year end, makes a loan of £12,000 to Jim who is a full time working director and holds 3% of the share capital on 1 October 2010. On the 1 January 2011 Jim repays £5000 of the loan. On the 31 March 2011 Jim increases his shareholding to 6%.

At the time of the loan it is covered by the exception as it is for less than £15,000, and to a full-time working director who does not hold a material interest in the company. No s.455 tax is payable.

The repayment of £5,000 has no implications for s.455.

On 31 March 2011 Jim acquired further shares and now holds more than 5%. Thus Green Ltd is treated as having made a loan on 31 March 2011 equal to the loan outstanding which is £12,000 - £5,000 = £7,000.

S.455 tax is payable in respect of the chargeable accounting period ended 31 December 2011. If the company is not large it will be due on 1 October 2012.

29.2 Beneficial loan interest

[CTA 2010,
s.1064](#)

Where a **company makes a loan to a participator**, and either **charges no interest**, or **charges interest below the official rate**, a **benefit in kind is levied on the participator**. Where the participator is an employee or director this will need to be reported on his P11D and will be taxed under the earnings rules.

Illustration 2

Campbell Ltd, a close company, lends £10,000 to Ted who is a shareholder and employee in the company. The loan is advanced on 1 October 2009 and Ted repays it to Campbell Ltd on 30 September 2010. Assuming that the beneficial interest rate is 7.25%, Ted's benefit in kind will be as follows.

For the tax year 2009/10, we look at the period 1 October 2009 to 5 April 2010 which is 187 days and therefore the benefit will be:

$$£10,000 \times 7.25\% \times \frac{187}{365} = £371$$

For the next tax year 2010/11, we look at the period 6 April 2010 to 30 September 2010, that is a period of 178 days, and therefore the benefit will be:

$$£10,000 \times 7.25\% \times \frac{178}{365} = £354$$

These figures will need to be reported on Ted's P11Ds for those separate tax years.

29.3 Benefits to participators

[CTA 2010,
s.1065](#)

Where a shareholder is an employee or director of a close company, any benefits he receives are taxed under the earnings rules. Therefore, in the absence of any special rules, where shareholders are not directors or employees, they would not pay any tax on benefits they receive. This is the reason for **S.1064 which will treat those benefits as net dividends paid to those shareholders**. The net dividend is calculated using the normal benefit rules for earnings.

S.1064 applies to any expense incurred by the company in connection with the provision of living or other accommodation, entertainment, domestic or other services or other benefits or facilities of whatever nature.

S.1064 does not include:

- 1) Benefits to employees which are taxed under the earnings rules;
- 2) Living accommodation if it is within the exceptions within the earnings rules;
- 3) Pensions, annuities or lump sums paid to the children, spouse or dependants of an employee on the employee's death or retirement.

Illustration 3

Joan receives a company car from Morley Ltd, a close company. The car has a list price of £21,000, and CO₂ emissions of 183g/km. She is a shareholder in the company but not an employee or a director. In tax year 2010/11, she will be treated as receiving a net dividend calculated using the employment benefit rules. Joan pays tax at the additional rate of 50%.

	£
Car Benefit	
$[180 - 135]/5 = 9 + 15 = 24\%$	
$£21,000 \times 24\% = £5,040$	
Deemed gross dividend	<u>5,600</u>
$£5,040 \times \frac{100}{90}$	
Tax at 42.5%	2,380
Tax credit: $£5,600 \times 10\%$	<u>(560)</u>
Higher rate tax due	<u>1,820</u>

That gives us a net dividend of £5,040 which we gross up at 100/90 to £5,600.

The tax will be added to Joan's tax liability for 2010/11 and the tax must be paid by 31 January 2012.

29.4 Close investment holding companies

All close companies are Close Investment Holding Companies (CIHCs) unless they exist wholly or mainly for one of the permitted purposes, which basically are to be a trading company, or a member of a trading group, or to make investments in land.

[CTA 2010, s.34](#)

Where the company is a CIHC, it **cannot use the small and marginal company rates of tax**. Instead such companies will **always be taxed at the full rate** of corporation tax (currently 28%, for FY2011 27%), regardless of the level of its profits.

29.5 Jointly held property

Where shares in a close company are held jointly by a husband and wife any **income from the shares will be taxed according to actual ownership**. Previously the income was taxed 50:50 unless an election was made for taxation according to actual ownership.

29.6 Summary

Where a **benefit is paid to an employee or director**, as far as the recipient is concerned, the benefit is taxed in the usual way under the earnings rules and reported on **form P11D**. As far as the company is concerned, the cost of providing that benefit is tax deductible in the usual way.

As far as a non-working participator recipient is concerned, the individual will be **treated as receiving a dividend on any s.1064 benefits received**. The value of the dividend will be calculated using the normal benefit rules and will be subject to higher rate tax where appropriate.

As far as the company is concerned, the cost of providing that benefit will **not be deductible** as it is treated as an appropriation from profit.

The exception to this rule is **the write off of a loan to a participator**. A loan write off is **always treated as a distribution**.